

New Issue
Book-Entry Only

Ratings: Moody's: Aaa (Underlying Aa3)
Standard & Poor's: AAA (Underlying A)

In the opinion of Bond Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended, that must be satisfied subsequent to the issue date of the Bonds, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals. However, while interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by certain S corporations may be subject to tax, and interest on the Bonds received by foreign corporations with United States branches may be subject to a foreign branch profits tax. Receipt of interest on the Bonds may have other federal tax consequences for certain taxpayers. See "Tax Exemption" and "Certain Other Federal Tax Consequences" under "Legal and Tax Information" herein.

\$251,850,000

THE CITY OF SEATTLE, WASHINGTON

MUNICIPAL LIGHT AND POWER IMPROVEMENT AND REFUNDING REVENUE BONDS, 2003

Dated: Date of Initial Delivery

Due: November 1, as shown on inside cover

The Bonds will be issued as fully registered bonds under a book-entry only system, registered in the name of Cede and Co. as registered owner and nominee for DTC. DTC will act as initial securities depository for the Bonds. Individual purchases of the Bonds will be made in book-entry form, in the denomination of \$5,000 or any integral multiple thereof. Purchasers will not receive certificates representing their interests in the Bonds. Interest on the Bonds will be paid semiannually on each May 1 and November 1, beginning November 1, 2003. The principal of and interest on the Bonds are payable by the Bond Registrar (currently, The Bank of New York in New York, New York) to DTC, which in turn is obligated to remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds, as described in "Description of the Bonds—Book-Entry Transfer System" and in Appendix E.

MATURITY SCHEDULE LOCATED ON INSIDE COVER

The Bonds are being issued to (i) finance certain capital improvements to and conservation programs for the Light System, (ii) refund certain of the City's Outstanding Parity Bonds, and (iii) to pay the costs of issuance of the Bonds. See "Plan of Finance."

The Bonds are subject to optional and mandatory redemption prior to maturity as described herein. See "Description of the Bonds—Redemption of the Bonds."

The Bonds are special limited obligations of the City payable from and secured solely by the Gross Revenues of the Light System and by money in the Parity Bond Fund and the Reserve Fund. The Bonds will be issued on a parity with \$1,309,961,000 of Outstanding Parity Bonds, of which \$118,895,000 will be refunded by the Bonds, and any Future Parity Bonds. The Gross Revenues are pledged to make the required payments into the Parity Bond Fund and the Reserve Fund; this pledge is superior to all other charges upon the Gross Revenues except for reasonable charges for maintenance and operation of the Light System. Maintenance and operation charges include the unconditional obligation of the City to make payments under certain power purchase contracts, as more fully described in "Power Resources—Purchased Power Arrangements." See "Security for the Bonds."

The Bonds do not constitute general obligations of the City, the State of Washington or any political subdivision of the State, or a charge upon any general fund or upon any money or other property of the City, the State or any political subdivision of the State not specifically pledged thereto by the Bond Ordinance. Neither the full faith and credit nor the taxing power of the City, nor any revenues of the City derived from sources other than the Light System, are pledged to the payment of the Bonds.

The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by Financial Security Assurance Inc. See "Other Bond Information—Municipal Bond Insurance."



The Bonds are offered for delivery when, as and if issued, subject to the approving legal opinion of Foster Pepper & Shefelman PLLC, Seattle, Washington, Bond Counsel, and certain other conditions. The form of Bond Counsel's opinion is attached hereto as Appendix B. It is expected that the Bonds will be available for delivery at the facilities of DTC in New York, New York, or to the Bond Registrar on behalf of DTC by Fast Automated Securities Transfer on or about August 20, 2003.

This cover page contains certain information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

Dated: July 29, 2003

\$251,850,000

THE CITY OF SEATTLE, WASHINGTON
MUNICIPAL LIGHT AND POWER IMPROVEMENT AND REFUNDING REVENUE BONDS, 2003

SERIAL BONDS

Due November 1	Amounts	Interest Rates	Yields	CUSIP Numbers
2004	\$ 9,915,000	6.00%	1.13%	8126427R1
2005	24,525,000	4.00	1.69	8126427S9
2006	22,745,000	5.00	2.00	8126427T7
2007	23,820,000	5.00	2.45	8126427U4
2008	11,875,000	5.00	2.80	8126427V2
2009	12,155,000	5.00	3.13	8126427W0
2010	12,770,000	5.00	3.55	8126427X8
2011	4,000,000	5.00	3.73	8126427Y6
2012	4,200,000	5.00	3.90	8126427Z3
2013	4,410,000	5.00	4.03	8126428A7
2014	4,630,000	5.25	4.15*	8126428B5
2015	9,545,000	5.25	4.25*	8126428C3
2016	10,045,000	5.25	4.35*	8126428D1
2017	10,570,000	5.25	4.45*	8126428E9
2018	11,125,000	5.25	4.54*	8126428F6
2019	5,980,000	5.25	4.61*	8126428G4
2020	6,295,000	5.25	4.70*	8126428H2
2021	6,625,000	5.00	4.90*	8126428J8
2022	6,955,000	5.00	4.96*	8126428K5
2023	7,300,000	5.00	5.01	8126428L3
2024	7,665,000	5.00	5.06	8126428M1
2025	8,050,000	5.00	5.09	8126428N9

TERM BONDS

2028	26,650,000	5.00%	5.07%	8126428P4
------	------------	-------	-------	-----------

* Priced to the November 1, 2013, par call date.

THE CITY OF SEATTLE

CITY OFFICIALS AND CONSULTANTS

MAYOR AND CITY COUNCIL

Greg Nickels	Mayor
Peter Steinbrueck	President, City Council
Jim Compton	Council Member
Richard Conlin	Council Member
Jan Drago	Council Member
Nick Licata	Council Member
Richard McIver	Council Member
Judy Nicastro	Council Member
Margaret Pageler	Council Member
Heidi Wills	Council Member

SEATTLE CITY LIGHT DEPARTMENT

James P. Ritch	Acting Superintendent
Jesse A. Krail, P.E.	Deputy Superintendent, Distribution
Dana L. Backiel	Deputy Superintendent, Generation
Carol K. Everson	Acting Deputy Superintendent, Finance and Administration
Joan Walters	Deputy Superintendent, Customer Services
Mike Sinowitz	Deputy Superintendent, Power Management

CITY ADMINISTRATION

Dwight D. Dively	Director of Finance
Thomas A. Carr	City Attorney

BOND COUNSEL

Foster Pepper & Shefelman PLLC
Seattle, Washington

FINANCIAL ADVISOR

Seattle-Northwest Securities Corporation
Seattle, Washington

No dealer, broker, salesperson, or other person has been authorized by the City to give any information or to make any representations, other than as contained in this Official Statement, and if given or made, such other information or representations must not be relied upon as having been authorized by the City. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy the Bonds, nor shall there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful for such persons to make such offer, solicitation or sale.

The information set forth herein has been furnished by the City, DTC and certain other sources that are believed to be reliable. The information and expressions of opinion contained herein are subject to change without notice. Any statements made in this Official Statement involving matters of opinion or estimates, whether or not so expressly stated, are set forth as such and not as representations of fact or representations that the estimates will be realized.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained under the caption "Bond Insurance" and Appendix F—Specimen Municipal Bond Insurance Policy herein, none of the information in this Official Statement has been supplied or verified by Financial Security and Financial Security makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information, (ii) the validity of the Bonds, or (iii) the tax exempt status of the interest on the Bonds.

Neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City since the date hereof.

This Official Statement is not to be construed as a contract with the purchasers of the Bonds.

The Bonds have not been registered under the Securities Act of 1933, as amended, in reliance upon a specific exemption contained in such act, nor have they been registered under the securities laws of any state.

TABLE OF CONTENTS

	<u>Page</u>
INTRODUCTION	1
PLAN OF FINANCE	1
The Bonds	1
Refunding Plan.....	2
Sources and Uses of Funds	2
SECURITY FOR THE BONDS	3
Pledge of Revenues.....	3
Outstanding Parity Bonds.....	3
Rate Covenant.....	3
Reserve Fund.....	3
Future Parity Bonds.....	4
Payment Agreements	4
No Acceleration of the Bonds	5
Subordinate Lien Bonds	5
Subordinate Lien Notes.....	5
Cash Pool Loan	5
Contingent Obligations	5
DESCRIPTION OF THE BONDS	5
Redemption of the Bonds.....	6
Open Market Purchase	6
Book-Entry Transfer System.....	6
THE DEPARTMENT	7
Introduction	7
Management.....	7
Employee Relations	8
Outstanding Debt and Debt Service Requirements	9
City Light System.....	11
Taxation and Intergovernmental Payments.....	11
Retail Rates	11
Billing and Collection Processes.....	18
Financial Policies	18
CUSTOMERS, ENERGY SALES AND PEAK LOADS	18
Service Area.....	18
Largest Customers.....	18
Historical Sales	19
Load Forecast (2003-2008).....	19
CHANGE IN THE ELECTRIC UTILITY INDUSTRY	21
Regional Transmission	21
Standard Market Design	21
Federal Energy Legislation	22
RECENT DEVELOPMENTS AFFECTING THE DEPARTMENT	22
Pending Litigation Before FERC	23
POWER RESOURCES.....	23
Overview of Resources	23
Resource Acquisitions	25
Resource Capabilities and Costs	26
The Department's Resources	31
Purchased Power Arrangements	32
Wholesale Market Sales and Purchases.....	38
Risk Management.....	40
Transmission	40
Conservation	41

TABLE OF CONTENTS (CONTINUED)

	<u>Page</u>
CAPITAL IMPROVEMENT AND CONSERVATION IMPLEMENTATION PROGRAMS	42
Generation.....	42
Transmission	42
Substations	42
Distribution	42
General Plant	42
High Ross Payment Amortization	43
Conservation	43
Other Potential Capital Projects	43
Financing.....	43
HISTORICAL AND PROJECTED OPERATING RESULTS	45
Historical Results—2000-2002	45
Projected Results—2003	46
Projected Results—2004-2008	48
Uncertainty of Projections and Potential Mitigating Actions	48
ENVIRONMENTAL MATTERS	53
Impact of Environmental Matters	53
Waste Management and Disposal Issues	53
Contaminated Site Liability	53
Endangered Species Act Issues.....	54
Clean Water Act Issues	55
Renewable Energy and Carbon Dioxide Mitigation.....	55
Electromagnetic Fields.....	55
THE CITY OF SEATTLE	56
Municipal Government.....	56
Financial Management.....	56
Risk Management.....	57
Pension System.....	57
Labor Relations	58
INITIATIVE AND REFERENDUM.....	58
LEGAL AND TAX INFORMATION	58
Bond Litigation	58
Approval of Counsel.....	58
Tax Exemption	58
Certain Other Federal Tax Consequences	59
Continuing Disclosure Undertaking	61
OTHER BOND INFORMATION	63
Bond Insurance.....	63
Ratings on the Bonds	63
Purchaser of the Bonds	63
Official Statement	64
BOND ORDINANCE.....	APPENDIX A
FORM OF BOND COUNSEL OPINION	APPENDIX B
2002 AUDITED FINANCIAL STATEMENTS OF THE DEPARTMENT	APPENDIX C
DEMOGRAPHIC AND ECONOMIC INFORMATION.....	APPENDIX D
BOOK-ENTRY TRANSFER SYSTEM	APPENDIX E
SPECIMEN MUNICIPAL BOND INSURANCE POLICY	APPENDIX F

OFFICIAL STATEMENT

\$251,850,000

THE CITY OF SEATTLE, WASHINGTON MUNICIPAL LIGHT AND POWER IMPROVEMENT AND REFUNDING REVENUE BONDS, 2003

INTRODUCTION

The purpose of this Official Statement, which includes the cover page and the appendices, is to set forth certain information concerning The City of Seattle (the “City”), its City Light Department (the “Department” or “City Light”), municipal light and power plant and system (the “Light System”), and Municipal Light and Power Improvement and Refunding Revenue Bonds, 2003 (the “Bonds”), in connection with the offering and sale of the Bonds. The Bonds are to be issued in accordance with Ordinance 121198 passed on June 23, 2003 (the “Bond Ordinance”), and Resolution 30618, adopted on July 29, 2003 (the “Bond Resolution”).

The Bond Ordinance is attached hereto as Appendix A. Appendix B contains the form of legal opinion of Foster Pepper & Shefelman PLLC (“Bond Counsel”). Appendix C contains the Department’s audited 2002 financial statements. Appendix D provides demographic and economic information about the City. Appendix E contains information on the Book-Entry Transfer System supplied by DTC and the City. Appendix F is a specimen municipal bond insurance policy. Capitalized terms that are not defined herein have the meanings set forth in the Bond Ordinance and Bond Resolution.

The Bonds are being issued on a parity of lien with the City’s senior lien Municipal Light and Power Revenue Bonds, which include 12 series of bonds issued since 1993 (the “Outstanding Parity Bonds”). As of May 31, 2003, the City had \$1,309,961,000 principal amount of Outstanding Parity Bonds, of which \$118,895,000 will be refunded by the Bonds. See “Plan of Finance—Refunding Plan.”

In the preparation of the projections in this Official Statement, the City has made certain assumptions with respect to conditions that may occur in the future. While the City believes these assumptions are reasonable for the purpose of the projections, they depend upon future events, and actual conditions may differ from those assumed. The City does not represent or guarantee that actual results will replicate the estimates in the various tables set forth in this Official Statement. The electric industry has undergone significant changes, as discussed in this Official Statement. Potential purchasers of the Bonds should not rely on the projections in this Official Statement as statements of fact. Such projections are subject to change, and will change, from time to time. The City has not committed itself to provide investors with updated forecasts or projections.

Neither the Department’s independent auditors, nor any other independent accountants, have compiled, examined or performed any procedures with respect to the projected financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and assume no responsibility for, and disclaim any association with, the prospective financial information.

PLAN OF FINANCE

The Bonds

The Bonds are being issued to (i) finance certain capital improvements to and conservation programs for the Light System (the “Plan of Additions”), (ii) refund certain of the City’s Outstanding Parity Bonds, as described under “Plan of Refunding,” and (iii) pay the costs of issuance of the Bonds.

Refunding Plan

A portion of the proceeds from the sale of the Bonds will be used to refund a portion of the City's outstanding Municipal Light and Power Revenue and Refunding Bonds, 1993, described below (the "Refunded Bonds"). The Refunded Bonds will be called on November 1, 2003.

REFUNDED BONDS

	Maturity	Amount (\$)	Interest Rate (%)	Call Price
Serials	11/01/2004	8,310,000	5.000	102
	05/01/2005	21,215,000	5.100	102
	11/01/2005	465,000	5.100	102
	05/01/2006	20,000,000	5.200	102
	05/01/2007	21,020,000	5.300	102
	05/01/2008	8,675,000	5.400	102
Term	11/01/2010	18,170,000	5.450	102
	11/01/2018	21,040,000	5.375	101
Total		118,895,000		

From the proceeds of the Bonds and other available money, the City will purchase direct, noncallable obligations of the United States (the "Acquired Obligations"). These Acquired Obligations will be deposited in the custody of U.S. Bank National Association or a duly appointed successor (the "Refunding Trustee"). The Acquired Obligations, interest earned thereon and any necessary beginning cash balance will be used to provide for the payment of the Refunded 1993 Bonds, pursuant to a refunding trust agreement to be executed by the City and the Refunding Trustee.

The mathematical accuracy of (i) the computations of the adequacy of the maturing principal amounts of and interest on the Acquired Obligations to be held by the Refunding Trustee to pay principal and interest and the redemption premium, if any, on the Refunded Bonds as described above, and (ii) the computations supporting the conclusion of Bond Counsel that the Bonds are not "arbitrage bonds" under Section 148 of the Internal Revenue Code of 1986, as amended, will be verified by Grant Thornton LLP, independent certified public accountants.

Sources and Uses of Funds

The proceeds of the Bonds are expected to be applied as follows:

Sources of Funds

Par Amount of the Bonds	\$ 251,850,000
Net Original Issue Premium	14,546,156
Total Sources of Funds	<u>\$ 266,396,156</u>

Uses of Funds

Construction Fund Deposit	\$ 140,000,000
Escrow Deposit	123,967,452
Costs of Issuance* and Additional Proceeds	2,428,704
Total Uses of Funds	<u>\$ 266,396,156</u>

- * Includes legal fees, financial advisory fees, rating agency and printing costs, underwriter's discount, bond insurance premium, and certain miscellaneous expenses.

SECURITY FOR THE BONDS

Pledge of Revenues

The Bonds are special limited obligations of the City. The principal of and interest on the Bonds are payable out of the Seattle Municipal Light Revenue Parity Bond Fund (the “Parity Bond Fund”). The City has agreed to pay into the Parity Bond Fund on or prior to the respective dates on which principal of and premium, if any, and interest on Parity Bonds will be payable, certain amounts from the Gross Revenues of the Light System sufficient to pay such principal and interest as the same become due. The Gross Revenues of the Light System are pledged to make such payments, which pledge constitutes a lien and charge upon such revenues prior and superior to all other charges whatsoever except reasonable charges for maintenance and operation of the Light System. See Appendix A—Bond Ordinance—Sections 16 and 17(a). Gross Revenues include the proceeds received by the City directly or indirectly from the sale, lease or other disposition of any of the properties, rights or facilities of the Light System, but do not include Bond proceeds and certain insurance proceeds. See Appendix A—Bond Ordinance—Section 1. Maintenance and operation charges do not include any taxes paid to the City (see “The Department—Taxation and Intergovernmental Payments”), but do include the unconditional obligation to make payments under certain power purchase contracts. See “Contingent Obligations” below.

Payment of the principal of and premium, if any, and interest on Parity Bonds constitutes a first and prior lien upon Gross Revenues of the Light System, after payment of reasonable maintenance and operation costs, superior to payments of principal of and premium, if any, and interest on the outstanding 2002 Notes and the Subordinate Lien Bonds, all described below, unless and until such Subordinate Lien Bonds are converted to fixed rate Parity Bonds in compliance with the requirements for the issuance of additional Parity Bonds.

The Bonds do not constitute general obligations of the City, the State of Washington (the “State”) or any political subdivision of the State, or a charge upon any general fund or upon any money or other property of the City, the State or any political subdivision of the State not specifically pledged thereto by the Bond Ordinance. Neither the full faith and credit nor the taxing power of the City, nor any revenues of the City derived from sources other than the Light System, are pledged to the payment of the Bonds.

Outstanding Parity Bonds

The Bonds are being issued on a parity of lien with the Outstanding Parity Bonds, which include 12 series of bonds issued since 1993. As of June 30, 2003, the City had \$1,309,961,000 principal amount of Outstanding Parity Bonds, of which \$118,895,000 will be refunded by the Bonds. See “Refunding Plan.”

Rate Covenant

In the Bond Ordinance the City has covenanted, among other things, to establish and maintain rates sufficient to provide for payment of debt service on the Outstanding Parity Bonds and any additional bonds issued on a parity of lien with the Outstanding Parity Bonds (the “Future Parity Bonds” and, together with the Outstanding Parity Bonds, the “Parity Bonds”) and all other obligations for which revenues have been pledged or to provide for such payment from other sources, to pay all costs of maintenance and operation and to maintain the Light System in good order and repair. The Bond Ordinance does not include a requirement that the City set rates to achieve a specific level of debt service coverage on Parity Bonds. See “The Department—Financial Policies” and Appendix A—Bond Ordinance—Section 17(d).

Reserve Fund

The City has created and is required to maintain the Municipal Light and Power Bond Reserve Fund (the “Reserve Fund”). The City has covenanted and agreed that it will pay into the Reserve Fund, out of Gross Revenues, within five years from the date of issuance of the Bonds, such sums as will, together with money presently in the Reserve Fund, provide for the Reserve Fund Requirement, which is defined as an amount equal to the lesser of:

- (i) the maximum Annual Debt Service on all Parity Bonds then outstanding, and

- (ii) the maximum amount permitted by the Internal Revenue Code of 1986, as amended, as “a reasonably required reserve or replacement fund.”

On the New Covenant Date, as defined in the Bond Ordinance, “Reserve Fund Requirement” will mean, for any issue of Parity Bonds, the Reserve Fund Requirement specified for that issue, and the Reserve Fund Requirement for all series of Parity Bonds will be the sum of the Reserve Fund Requirements for all such Parity Bonds.

If payments from the Reserve Fund are required to pay interest on or principal of any Outstanding Parity Bonds, the City will deposit money into that fund out of any money legally available therefor until the Reserve Fund has been replenished to the Reserve Fund Requirement. The balance in the Reserve Fund as of June 30, 2003, was \$79,265,992. Additional amounts will be deposited over the next five years to satisfy the Reserve Fund Requirement for the Parity Bonds.

In lieu of cash deposits to the Reserve Fund, the City may provide Qualified Insurance or a Qualified Letter of Credit in an amount equal to the Reserve Fund Requirement or any portion thereof. See Appendix A—Bond Ordinance—Section 17(b)(i).

Future Parity Bonds

The Bond Ordinance authorizes the issuance of additional Parity Bonds subsequent to the issuance of the Bonds (the “Future Parity Bonds”) if:

- (i) there is no deficiency in the Parity Bond Fund or in any of the accounts therein and provision has been made to meet the Reserve Fund Requirement for all Parity Bonds then outstanding plus the proposed Future Parity Bonds, and
- (ii) either:
 - (a) the Finance Director certifies that Gross Revenues (with certain adjustments), less the expenses of operation, maintenance and repair of the Light System (the “Net Revenue”), in any 12 consecutive months out of the most recent 24 months preceding the issuance of the Future Parity Bonds (the “Base Period”) were not less than 125 percent of maximum Annual Debt Service in any future calendar year on all Parity Bonds then outstanding and the Future Parity Bonds proposed to be issued, or
 - (b) the City has on file a certificate of a Professional Utility Consultant stating that the Adjusted Net Revenue for the Base Period, calculated as described in the Bond Ordinance, was not less than 125 percent of maximum Annual Debt Service in any future calendar year on all Parity Bonds then outstanding and the Future Parity Bonds proposed to be issued. The Bond Ordinance permits the Professional Utility Consultant to adjust Net Revenue based on certain conditions.

On the New Covenant Date, “Net Revenue” will mean, for the purpose of these requirements for the issuance of Parity Bonds, that amount determined by deducting from Gross Revenues the expenses of operation, maintenance and repair of the Light System and further deducting any deposits into the Rate Stabilization Account and by adding to Gross Revenues any withdrawals from the Rate Stabilization Account. See Appendix A—Bond Ordinance—Section 17(g).

The Bond Ordinance authorizes the issuance of Refunding Parity Bonds without the requirement of meeting the above provisions. See Appendix A—Bond Ordinance—Section 17(h).

Payment Agreements

The City may enter into Parity Payment Agreements that constitute a charge and lien on Net Revenue equal to that of the Parity Bonds. The prerequisites described above for the issuance of Future Parity Bonds apply to the City’s incurrence of obligations under any Parity Payment Agreements. See Appendix A—Bond Ordinance—Section 1—Definitions—Annual Debt Service.

No Acceleration of the Bonds

The Bonds are not subject to acceleration upon the occurrence of a default. The City, therefore, would be liable only for principal and interest payments as they become due. In the event of multiple defaults in payment of principal or interest on the Parity Bonds, the registered owners would be required to bring a separate action for each such payment not made. This could give rise to a difference in interests between registered owners of earlier and later maturing Parity Bonds.

Subordinate Lien Bonds

The City had \$98,355,000 principal amount of outstanding Subordinate Lien Bonds as of June 30, 2003, all in variable rate mode. The ordinances authorizing the issuance of the Subordinate Lien Bonds allow for the conversion of those bonds to Parity Bonds upon compliance with the requirements relating to the issuance of additional Parity Bonds at the time of conversion. Under the authorizing ordinances, the aggregate principal amount of outstanding Subordinate Lien Bonds at the time of issuance is limited to the greater of \$70,000,000 or 15 percent of the aggregate principal amount of Parity Bonds then outstanding.

Subordinate Lien Notes

Also outstanding on May 31, 2003, was \$125,000,000 principal amount of Municipal Light and Power Revenue Anticipation Notes, 2002 (the “2002 Notes”), which mature on November 21, 2003. The lien of the 2002 Notes on Net Revenue is subordinate to the lien on such Net Revenue of the Parity Bonds and the Subordinate Lien Bonds.

Cash Pool Loan

The City’s Director of Finance is authorized to make loans to individual funds participating in the City’s common investment portfolio (the “Cash Pool”) by carrying such funds in a negative cash position for a period of up to 90 days, or for a longer period upon approval by the City Council by ordinance, to the extent such loans can be supported prudently by the Cash Pool and the borrowing fund is reasonably expected to be able to repay the loan. Such loans bear interest at the Cash Pool’s rate of return. In May 2003, the City Council passed an ordinance authorizing a loan of up to \$50 million to the operating account of the Light Fund from the Cash Pool through August 31, 2003. As of July 7, 2003, this loan had been repaid in full. The ordinance also authorized the Light Fund to borrow \$100 million from the Cash Pool for the period from October 31, 2003, through December 31, 2004. The Department expects to make use of this authorization from November 2003 through June 2004. The maximum amount of the Department’s indebtedness to the Cash Pool is projected to be \$71 million in December 2003. See “The City of Seattle—Financial Management—Interfund Loans.”

Contingent Obligations

The Department has in the past and may in the future enter into various agreements, such as energy purchase agreements or financial derivative contracts, under which the Department may be obligated to make payments or post collateral contingent upon certain future events within or beyond the Department’s control. Such contingent payment obligations may be treated as operation and maintenance charges payable from Gross Revenues prior to the payment of principal of and interest on the Parity Lien Bonds, the Subordinate Lien Bonds and the 2002 Notes. See “Power Resources—Purchased Power Arrangements.”

DESCRIPTION OF THE BONDS

The Bonds will be dated the date of their initial delivery. Interest on the Bonds is payable semiannually on each May 1 and November 1, beginning November 1, 2003, at the rates set forth on the inside cover of this Official Statement. Principal is payable on each November 1, beginning November 1, 2004, in the amounts set forth on the inside cover of this Official Statement. Interest on the Bonds is to be computed on the basis of a 360-day year consisting of twelve 30-day months. The Bonds will be issued in \$5,000 denominations and integral multiples thereof. The principal of and interest on the Bonds is payable by the Bond Registrar, currently the fiscal agent of the State of Washington (the “Bond Registrar”) (currently, The Bank of New

York in New York, New York). For so long as the Bonds remain in a “book-entry only” transfer system, the Bond Registrar will make payments of principal and interest only to DTC, which in turn will remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds, as further described in Appendix E hereto.

Redemption of the Bonds

Optional Redemption. The Bonds maturing before November 1, 2014, are not subject to redemption prior to maturity. The Bonds maturing on or after November 1, 2014, are subject to redemption prior to maturity at the option of the City on and after November 1, 2013, in whole or in part at any time (maturities to be selected by the City and randomly within a maturity in such manner as the Bond Registrar may determine and, so long as the Bonds are in book-entry form, in accordance with the procedures established by the securities depository) at the price of par plus accrued interest.

Mandatory Redemption. If not previously redeemed as described above, the Term Bonds will be called for redemption (in such manner as DTC will determine) at a price of par plus accrued interest to the redemption date, on November 1 in the years and amounts shown below.

<u>Year</u>	<u>Amount</u>
2026	\$8,455,000
2027	8,875,000
2028*	9,320,000

* Final maturity.

If the City redeems Term Bonds under the optional redemption provisions described above or purchases Term Bonds in the open market as described below, the par amount of the Term Bonds so redeemed or purchased (irrespective of their actual redemption or purchase prices) will be credited against the remaining scheduled mandatory redemption requirements for those Term Bonds in a manner to be determined by the City or, if no such determination is made, on a pro-rata basis.

Notice of Redemption. Notice of any intended redemption will be given not less than 30 nor more than 60 days prior to the redemption date by first-class mail, postage prepaid, to the registered owner of any Bond to be redeemed at the address appearing on the Bond Register at the time the Bond Registrar prepares the notice. The requirements of this section will be deemed to have been fulfilled when the notice is mailed, whether or not it actually is received by the registered owner of any Bond. As long as the Bonds are held in book-entry form, notices will follow procedures established by the securities depository. See “Description of the Bonds—Book-Entry Transfer System.”

Open Market Purchase

The City reserves the right and option to purchase any or all of the Bonds in the open market at any time at any price acceptable to the City plus accrued interest to the date of purchase.

Book-Entry Transfer System

Book-Entry Bonds. DTC will act as initial securities depository for the Bonds. The ownership of one fully registered Bond for each maturity, as set forth on the inside cover of this Official Statement, each in the aggregate principal amount of such maturity, will be registered in the name of Cede and Co., as nominee for DTC. For so long as the Bonds remain in a “book-entry only” transfer system, the Bond Registrar will make payments of principal and interest only to DTC, which in turn will remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds. See Appendix E for additional information. *As indicated therein, certain information in Appendix E has been provided by DTC. The City makes no representation as to the accuracy or completeness of the information in Appendix E provided by DTC. Purchasers of the Bonds should confirm this information with DTC or its participants.*

Termination of Book-Entry Transfer System. If DTC resigns as the securities depository and the City is unable to retain a qualified successor to DTC, or if the City determines that a continuation of the book-entry transfer

system is not in the best interests of the City, the City will deliver at no cost to the beneficial owners of the Bonds or their nominees Bonds in registered certificate form, in the denomination of \$5,000 or any integral multiple thereof within a maturity. Thereafter, the principal of the Bonds will be payable upon due presentment and surrender thereof at the principal office of the Bond Registrar. Interest on the Bonds will be payable by check or draft mailed or by wire transfer (wire transfer will be made only if so requested in writing and if the registered owner owns at least \$1,000,000 par value of the Bonds), to the persons in whose names such Bonds are registered, at the address appearing upon the registration books on the 15th day of the month preceding an interest payment date, and the Bonds will be transferable as provided in the Bond Ordinance.

THE DEPARTMENT

Introduction

The Department is a municipally-owned electric utility. In 1905, the City began providing its residents with electricity generated by the Cedar Falls Hydroelectric Plant, which was the first municipally-owned hydroelectric facility in the nation. By 1910, operational responsibility for the City's electric system had been assigned to a separate lighting department, referred to herein as the "Department." In 1951, the Department purchased from Puget Sound Power and Light Company certain generation, transmission and distribution facilities serving the City's residents. The Department has operated without competition in its service area since the 1951 purchase. See "Customers, Energy Sales and Peak Loads—Service Area" for a description of the Department's service area.

The Light System currently consists of seven hydroelectric generating plants (with an aggregate one-hour peak capability of approximately 1,800 MW), approximately 656 miles of transmission lines (through which electricity is wheeled to and between the Department's various substations), over 2,400 miles of distribution lines (through which electricity is delivered from such substations to customers), 14 major substations, and two service centers. See "City Light System" and "Power Resources" for a discussion of the Department's existing facilities and "Capital Improvement and Conservation Implementation Programs" for a discussion of the Department's proposed capital projects. The Light System is interconnected with transmission lines owned by the Bonneville Power Administration ("Bonneville"). See "Power Resources—Transmission" for a discussion of Bonneville's transmission system.

Management

The Department is a department of the City and is subject to ordinances and resolutions adopted by the City Council and approved by the Mayor. The Mayor and City Council approve the Department's budget, set rates and approve financing and bond issuance, along with other functions outlined in the City Charter. The Department is under the direction of a superintendent, who is appointed by the Mayor and confirmed by the City Council. Currently the Department is headed by an acting superintendent on an interim basis. A process to select a permanent superintendent is in progress and is expected to be completed within the next twelve months.

In October 2002, a panel appointed by the Mayor recommended the establishment of an advisory board consisting of individuals with experience in the utility industry to provide advice to the Mayor and the City Council on policy and management issues facing the Department. In January 2003, the City Council passed an ordinance calling for the appointment of a six-member City Light Advisory Board. The Mayor and the City Council each designated three individuals to serve on the Board in March 2003, and the Board held its first meeting the following month. The responsibilities of the Board are purely advisory.

The Department is organized into four main operating branches (Generation, Distribution, Power Management, and Customer Services) which are headed by Deputy Superintendents who report directly to the Superintendent. A Deputy Superintendent for Finance and Administration, also reporting to the Superintendent, has responsibility for the Department's major administrative functions, including Finance, Information Technology and Facilities. Division Directors responsible for the Human Resources Division, Environment and Safety Division, Strategic Planning Office, and External Affairs Office also report directly to the Superintendent.

Brief descriptions of the backgrounds of certain key officials of the Department are provided below:

James P. Ritch, Acting Superintendent, was appointed to his current position in April 2003. Prior to his appointment, Mr. Ritch had served as Deputy Superintendent for Finance and Administration since 1994. Mr. Ritch has held various other positions in City government, including Director of the Office of Management and Budget and Director of the Department of Administrative Services. Mr. Ritch also was the Vice President of Human Resources for Egghead Software. Mr. Ritch received Bachelor of Arts and Master of Arts degrees in economics from the University of Washington.

Jesse A. Krail, P.E., Deputy Superintendent, Distribution, was appointed to his current position in 1996. Mr. Krail is responsible for management of the Distribution Branch, which delivers power and electrical services, including transmission, substations, feeders, and meters, to customers. Mr. Krail has extensive experience in public works and a broad management, engineering and customer service background with large public agencies, including the King County Department of Public Works/Transportation and the Seattle Engineering Department. Mr. Krail holds a Bachelor of Science degree in electrical engineering from Union College, New York. He is a Licensed Civil Engineer in the State of Washington.

Dana L. Backiel, Deputy Superintendent, Generation, was appointed to her current position in 1998. From her appointment to Chief Engineer in 1996 until her present appointment, Ms. Backiel managed all in-house engineering service functions. Previously, Ms. Backiel held the position of Power Stations Director and served as Acting North Electric Services Director. Ms. Backiel obtained her bachelor's degree in electrical engineering from Case Institute of Technology (Case/Western Reserve University) in Cleveland, Ohio.

Carol K. Everson, Acting Deputy Superintendent, Finance and Administration, was appointed to the position of chief financial officer for the Department in April 2003. Ms. Everson has worked for the Department since 1985 as an economist, budget manager, rates manager, and, most recently, as Director of Finance. Ms. Everson received a Bachelor of Arts degree from Vassar College and master's and doctoral degrees in economics from the University of Toronto.

Joan Walters, Deputy Superintendent, Customer Services, was appointed to her current position in January 2002. Immediately prior to her appointment, Ms. Walters served as Budget Director for the City. During the 1990s, Ms. Walters held a number of positions with the State of Illinois, including Director of the Bureau of the Budget and Director of the Department of Public Aid. Ms. Walters holds a Bachelor of Arts degree in science from Governors State University in Illinois.

Mike Sinowitz, Deputy Superintendent, Power Management, served as Director of the City Light Power Control Center from June 1999 until his appointment to his current position in February 2002. Mr. Sinowitz joined the Department in 1987 as Manager of Generation, Transmission and Scheduling Dispatch at the System Control Center. He has over 30 years of experience in the utility industry, including positions with Pacific Gas & Electric, San Diego Gas & Electric and the Arabian-American Oil Company. Mr. Sinowitz holds a Bachelor of Science degree in electrical engineering from the University of California at San Diego.

Employee Relations

As of March 31, 2003, the Department had 1,618 full-time equivalent employees, almost all of whom are members of the City's Employee Retirement System. The Retirement System requires the Department, like all other City departments, to make contributions equal to an actuarially determined percentage of covered payrolls. See "The City of Seattle—Pension System."

State law requires municipal agencies to bargain collectively with formally recognized collective bargaining units. Currently, 14 union locals represent approximately 80 percent of the Department's regular full-time employees. The collective bargaining agreements between each of these unions and the Department will expire either on December 31, 2004, or on January 22, 2005. There have been no strikes during the past 20 years, and the Department considers its employee relations to be satisfactory. See "The City of Seattle—Labor Relations."

Outstanding Debt and Debt Service Requirements

As of June 30, 2003, there were outstanding \$1,309,961,000 in senior lien City of Seattle Municipal Light and Power Revenue Bonds (the "Parity Bonds"), \$98,355,000 in junior lien City of Seattle Municipal Light and Power Adjustable Rate Revenue Bonds (the "Subordinate Lien Bonds") and \$125,000,000 in 2002 Notes, due November 21, 2003, which are subordinate to the Parity Bonds and the Subordinate Lien Bonds. In addition, the City Council by ordinance in May 2003 authorized the Department to borrow up to \$50,000,000 from the City's Cash Pool through August 31, 2003, which was repaid in full as of July 7, 2003. The Department also is authorized to borrow up to \$100 million from the Cash Pool from October 31, 2003, through December 1, 2004.

Principal of and interest on the Parity Bonds, Subordinate Lien Bonds, Cash Pool loan, and 2002 Notes are payable from the gross revenues of the Light System, after payment of reasonable charges for maintenance and operation of the Light System. Maintenance and operation charges include the unconditional obligation to make payments under certain power purchase contracts.

Principal and interest payments due on the Department's outstanding Parity Bonds and Subordinate Lien Bonds are shown in the following table, which has been adjusted to show the estimated effects of the Refunding Plan. In addition to the amounts shown in the table, in 2003 the Department will pay \$125,000,000 in principal and \$3,125,000 in interest on the 2002 Notes.

DEBT SERVICE REQUIREMENTS

	Parity Bonds ⁽¹⁾			Subordinate Lien Bonds			All Bonds
Year	Principal	Interest	Total	Principal	Interest	Total	Total Debt Service
2003	\$ 37,030,000	\$ 68,689,316	105,719,316	\$ 3,585,000	\$ 1,719,331	\$ 5,304,331	\$ 111,023,647
2004	49,705,000	73,667,836	123,372,836	4,115,000	2,831,925	6,946,925	130,319,761
2005	52,781,000	71,551,004	124,332,004	4,445,000	3,850,608	8,295,608	132,627,612
2006	56,225,000	69,253,098	125,478,098	4,775,000	3,703,927	8,478,927	133,957,025
2007	58,945,000	66,524,335	125,469,335	5,305,000	3,572,170	8,877,170	134,346,505
2008	62,055,000	63,416,923	125,471,923	5,840,000	3,342,551	9,182,551	134,654,474
2009	65,365,000	60,115,898	125,480,898	6,270,000	3,075,680	9,345,680	134,826,578
2010	68,845,000	56,632,659	125,477,659	6,705,000	2,771,929	9,476,929	134,954,588
2011	64,310,000	53,223,983	117,533,983	7,345,000	2,722,544	10,067,544	127,601,527
2012	64,615,000	49,740,858	114,355,858	7,785,000	2,604,703	10,389,703	124,745,561
2013	67,410,000	46,150,081	113,560,081	8,425,000	2,262,284	10,687,284	124,247,365
2014	67,910,000	42,488,431	110,398,431	8,865,000	1,799,802	10,664,802	121,063,233
2015	68,380,000	38,796,188	107,176,188	9,410,000	1,331,760	10,741,760	117,917,948
2016	69,110,000	35,036,006	104,146,006	7,755,000	786,304	8,541,304	112,687,310
2017	69,230,000	31,253,800	100,483,800	2,600,000	518,751	3,118,751	103,602,551
2018	68,360,000	27,833,613	96,193,613	2,750,000	369,051	3,119,051	99,312,664
2019	65,395,000	24,163,725	89,558,725	1,300,000	207,744	1,507,744	91,066,469
2020	63,385,000	20,637,730	84,022,730	1,355,000	128,858	1,483,858	85,506,588
2021	61,175,000	17,288,663	78,463,663	1,410,000	43,590	1,453,590	79,917,253
2022	60,055,000	13,986,566	74,041,566				74,041,566
2023	59,805,000	10,747,524	70,552,524				70,552,524
2024	60,750,000	7,521,031	68,271,031				68,271,031
2025	44,480,000	4,434,148	48,914,148				48,914,148
2026	38,585,000	2,104,581	40,689,581				40,689,581
2027	8,875,000	909,750	9,784,750				9,784,750
2028	9,320,000	466,000	9,786,000				9,786,000
Total	<u>\$ 1,462,101,000</u>	<u>\$ 956,633,743</u>	<u>\$ 2,418,734,743</u>	<u>\$ 100,040,000</u>	<u>\$ 37,643,512</u>	<u>\$ 137,683,512</u>	<u>\$ 2,556,418,255</u>

(1) Reflects actual results of the sale of the Bonds.

City Light System

Power Resources. The Department owns and operates three major hydroelectric generating plants on the Skagit River, approximately 80 miles northeast of Seattle, and the Boundary Hydroelectric Plant (the “Boundary Project”) on the Pend Oreille River, approximately 250 miles east of Seattle. In addition, the Department owns three smaller hydroelectric plants in western Washington. The Department sold its eight percent share of the coal-fired Centralia Steam Plant to TransAlta Corporation in May 2000.

In addition to these resources, the Department’s power is supplied through contracts with Bonneville, two public utility districts and three Columbia Basin irrigation districts. Additional contracts are in place with King County, the Province of British Columbia, the City of Klamath Falls, Oregon, three Idaho irrigation districts, and one Oregon irrigation district. A long-term contract for the purchase of power from a wind-powered generation project in the Northwest region has been signed with PacifiCorp Power Marketing, Inc. (“PPM”).

More detailed information on the Department’s power resources is provided under “Power Resources” below.

Transmission Facilities. The Department operates a system of 656 miles of transmission facilities that follow several routes. Power from the Skagit River plants is transmitted over lines owned by the Department. The Department also uses the facilities of other agencies, principally Bonneville, to transmit power from other generating plants from which the Department receives power, including the Boundary Project. The Department’s transmission facilities are connected to Bonneville’s transmission grid. The Department also has acquired ownership rights to 160 MW of capacity over the AC Intertie, which connects the Pacific Northwest power grid with the Southwest region. See “Power Resources—Transmission.”

Distribution Facilities. There are 14 major substations in the Light System. Service in the City’s downtown business area and other areas of high load density is provided through underground network systems.

General Plant. The Department’s general plant facilities include two service centers that serve as headquarters for construction and maintenance activities, the System Control Center, communication facilities, transportation equipment, and office equipment, including data processing equipment. The System Control Center, completed in 1995, houses an advanced energy management system. The Department’s central administrative offices are located in Key Tower, a downtown Seattle office building owned by the City.

Taxation and Intergovernmental Payments

The Department pays a utility tax to the City equal to six percent of Gross Revenues from sales within the State. The proceeds of this tax are deposited into the City’s General Fund. The City Charter does not permit the Department to pay taxes to the City’s General Fund “until ample provision has been made for the servicing of the debts and obligations of the utility and for necessary betterments and replacements for the current year.” A State public utility tax is paid at a rate of 3.873 percent of Gross Revenues from sales within the State, less certain adjustments.

Certain contractual payments are made to Pend Oreille and Whatcom Counties, Washington, for services rendered. Under the terms of franchise agreements signed in 1998 and 1999, the Department makes monthly payments to the cities of Shoreline, Burien, Lake Forest Park, and SeaTac in amounts equal to six percent of the revenue attributable to the energy component of rates charged to customers residing within those cities. In April 2003, the Department signed a franchise agreement with the City of Tukwila that requires the Department to pay the City of Tukwila monthly amounts equal to four percent of the revenue billed to customers in Tukwila. See “The Department—Retail Rates.”

Retail Rates

Rate Setting. The City Council has exclusive jurisdiction with respect to establishing and revising the Department’s retail rates. State law requires that rates must be fair, nondiscriminatory and fixed to produce revenue that is adequate to pay operation and maintenance expenses of the Department and to meet all debt service requirements payable from such revenue. In its retail rate-setting capacity, the City Council is not

subject to control by the Washington Utilities and Transportation Commission, but it is subject to certain rate-making provisions of the Public Utility Regulatory Policies Act of 1978. The Department never has been cited for failing to comply with such act, and believes that it is operating in compliance with the act's requirements.

Since 1980 the City Council has conducted comprehensive reviews of the Department's rate levels and rate structure at intervals of two or three years. In the course of its rate reviews, the City Council holds public meetings to consider the Department's proposed budget, construction plan, load forecast, and resource plans. Based on these planning documents, as approved by the City Council, the Department's staff estimates the Department's revenue requirements and develops a rate proposal that will produce the required amount of revenue and that allocates the revenue requirement among the various rate classes in accordance with City policy. The City Council holds public meetings to introduce and explain the proposals to the public and to accept public input. The City Council makes final decisions through passage of a rate ordinance.

Rate Changes: 1990-1999. From 1990 through 1999, the City's periodic rate reviews resulted in the following changes in average rates for the system as a whole:

SUMMARY OF RATE CHANGES 1990-1999

<u>Effective Date</u>	<u>Percentage Change</u>
January 1, 1990	(2.4)%
May 1, 1993	12.6
March 1, 1995	5.7
March 1, 1996	5.3
March 6, 1997	(0.4)
March 1, 1998	(0.6)
December 24, 1999	3.2

In addition to these changes, the City Council imposed three temporary surcharges ranging from 4.1 percent to 10.0 percent between 1992 and 1995 to offset the impact of poor water conditions on power costs.

The most recent comprehensive rate review took place in 1999 and culminated in the passage of an ordinance in November 1999 that provided for an average increase of 3.2 percent, effective December 24, 1999. Pursuant to City policy, rates for low-income residential customers were set at levels 50 percent below rates in the standard residential classes. The ordinance provided for a further increase averaging 3.0 percent, effective March 1, 2002.

Rate Changes: 2000-2003. In 2000 and the first nine months of 2001, the Department was required to purchase large amounts of power in the wholesale market as a result of its 1996 decision to limit purchases of power from Bonneville (see "Power Resources—Purchased Power Arrangements"), the sale of the Centralia Steam Plant in May 2000 and unusually poor water conditions in the water year beginning October 1, 2000. Beginning in May 2000, largely as a result of supply constraints and the repercussions of restructuring efforts in California, wholesale market prices increased to unprecedented levels. As a result, the Department incurred power expenses in 2000 and 2001 that in total exceeded its budgeted estimates by almost \$600 million. See "Change in the Electric Utility Industry," "Recent Developments Affecting the Department" and "Historical and Projected Operating Results." In response to these developments, the City increased rates four times in 2001:

- (i) Effective January 1, 2001, all energy charges were increased by 0.4 cents per kWh, with the exception of rates for low-income customers, which were increased by 0.2 cents per kWh. On the average, rates increased by 9.8 percent.
- (ii) Effective March 1, 2001, winter energy charges for all classes except the low-income classes were increased by 0.4 cents per kWh and the distinction between summer rates and winter rates was eliminated. Rates for low-income customers remained unchanged. With rates for non-low-income

customers set at the higher winter levels in all months of the year, average rates increased by 18.0 percent.

- (iii) Effective July 1, 2001, energy charges for all classes except the low-income classes were increased by 0.49 cents per kWh, which represented an increase of 9.3 percent in average rates. Average rates for low-income customers were not increased, but effective October 1, 2001, the distinction between summer and winter rates for low-income customers was eliminated, and rates were set at the average of winter and summer rates.
- (iv) Effective October 1, 2001, all energy charges were increased by 0.6 cents per kWh, or 10.3 percent, with the exception of energy charges for the low-income rate classes, which received an increase of 0.3 cents per kWh. This increase passed through to customers the financial effect of increases in rates charged by Bonneville for transmission services and power purchases. Pass-through of the October 1, 2001, transmission and power rate increases had been mandated by the ordinances implementing the December 24, 1999, rate increases and the July 1, 2001, power cost adjustment, respectively. See “Power Resources—Purchased Power Arrangements.”

The last of the rate ordinances in 2001 also required that the effect of future increases or decreases in Bonneville rates be passed through to customer classes through adjustments to their energy charges. Pursuant to this provision, energy charges for all rate classes were reduced by 0.07 cents per kWh, effective April 1, 2002, except for the low-income rate classes, which were reduced by 0.04 cents per kWh. This resulted in an average decrease of 1.1 percent. Further rate adjustments by Bonneville were passed through to City Light customers on April 1, 2003, through an increase of 0.08 cents per kWh in energy charges for all classes except the low-income classes, which received an increase of 0.04 cents per kWh. The average rate increase on April 1, 2003, was 1.2 percent.

In addition to the four power cost adjustments enacted in 2001, rates for Medium and Large General Service customers in the downtown network were increased by 4.1 percent and 3.8 percent respectively, effective March 1, 2002, as provided for in the November 1999 rate ordinance. Fees for rental of streetlights, poles, ducts, and vaults also increased on that date. These increases resulted in an average increase of 0.5 percent for the system as a whole. The ordinance enacting the power cost adjustment effective July 1, 2001, eliminated the increases for the other rate classes that were to have taken effect on March 1, 2002, under the terms of the November 1999 ordinance.

Under the terms of the April 2003 franchise agreement between the City of Tukwila and the Department, customers in the City of Tukwila received rate increases averaging 4.7 percent to 5.6 percent, depending on the rate class, effective May 1, 2003. See “The Department—Rates Outside the City of Seattle.”

SUMMARY OF RATE CHANGES SINCE JANUARY 1, 2000

<u>Effective Date</u>	<u>Percentage Change</u>
January 1, 2001	9.8%
March 1, 2001	18.0
July 1, 2001	9.3
October 1, 2001	10.3
March 1, 2002	0.5
April 1, 2002	(1.1)
April 1, 2003	1.2
May 1, 2003	0.2

The net effect of the four power cost adjustments in 2001, the March 1, 2002, increase in network rates, the pass-through of the Bonneville rate adjustments on April 1, 2002, and April 1, 2003, and the increase in Tukwila rates has been to increase average rates for the system as a whole by 57 percent. Because low-income rates were exempted from the power cost adjustments effective March 1, 2001, and July 1, 2001, rates for low-income customers increased by about 20 percent.

Under the terms of the financial policies adopted by the City Council for the Department in December 2001, current rates will remain in effect until the Department repays all short-term debt obligations, including the 2002 Notes and the amounts borrowed from the Cash Pool, and accumulates an operating account cash balance of \$30 million, unless rates are increased by City Council action or adjusted to pass through further changes in Bonneville power rates. These conditions are expected to be met in mid-2004. At that point rates can be set in accordance with the rate-setting guidelines in the City Council-adopted financial policies, which give greater recognition to the higher risks that the Department faces in the current utility environment. The Department's financial forecast assumes that new rates will take effect on January 1, 2005. Financial policies adopted by the City Council are subject to change by the City Council. See "The Department—Financial Policies."

In 2002, the Department's average rate for residential service was 6.90 cents per kWh. The Department's commercial and industrial rates averaged 6.20 cents and 5.28 cents per kWh, respectively. See the table titled "Average Rates and Monthly Bills" for average rates and bills paid by the various customer classes. With the Department's recent power cost adjustments taken into account, the Department's current average rates are below the national average. See the table titled "Annual Bill Comparisons with Other Puget Sound Utilities" for a comparison of annual amounts paid by the Department's customers and the customers of neighboring utilities.

Rates Outside the City of Seattle. In 1998 and 1999, the cities of Shoreline, Lake Forest Park, SeaTac, and Burien granted franchises to the Department which recognized the right of the Department to set higher rates for customers located in those cities than the rates charged to Seattle customers. However, the differential between rates in Seattle and rates outside Seattle was limited to eight percent of the energy portion of rates, plus amounts required to recover the cost of service levels requested by any of the suburban cities that exceeded standard service levels provided by the Department. The rate ordinance that took effect in 1999 set rates for customers in these cities and in unincorporated King County at the maximum level permitted under the franchises. The franchise agreement then in effect between the Department and the City of Tukwila required the Department to charge the same rates in Tukwila as in Seattle. In April 2003, Tukwila granted a new franchise which contained rate provisions similar to those in the franchises with the other suburban cities. Rates in Tukwila were increased effective May 1, 2003.

Market-Indexed Rates for High Demand Customers. Since 1996, the Department has offered market-indexed rate schedules ("Market-Indexed Schedules") to the eight customers in its High Demand General Service classes. Currently no customers are served under the Market-Indexed Schedules.

Special Rates for New Large Loads. The City Council passed an ordinance in 2000 that created a new customer class for New Large Loads. A New Large Load is defined in the ordinance as any service fed from an expanded or a new installation equal to or greater than 12.5 megavolt-amperes ("MVA") of energized capacity installed within any consecutive five-year period after August 31, 2000. The ordinance provides that New Large Load customers will be charged for service either under the Department's Market-Indexed Schedule (see "The Department—Retail Rates—Market-Indexed Rates for High Demand Customers") or on the basis of a negotiated, customized delivery and payment package which would include one of a number of options for acquiring and paying for energy. New Large Loads will also pay a retail service charge to the Department for delivery of power to the customer's premises. Under either payment option, each New Large Load customer is responsible for installation costs and a fixed charge per MW of capacity to cover the cost of providing feeder and substation capacity. Currently no customers are being served as New Large Loads.

Interruptible Rates for High Demand Customers. In 2001, the City Council passed an ordinance creating a new rate class for High Demand General Service customers that sign contracts with the Department for interruptible service. Under the terms of such contracts, the Department has the right to interrupt service to such customers when the wholesale market price of energy exceeds a "trigger price," which has been set at \$55 per MWh through the end of 2003 and may be adjusted by the Department after that date. Through December 31, 2003, rates for High Demand customers choosing to be served on this basis have been set at levels approximately 30 percent below the rates for standard High Demand customers. Effective January 1, 2004, rates for this class will be the standard rates for customers in the High Demand class in the City of Seattle, plus 0.725 cents per kWh. This additional charge will remain in effect until the customer has

consumed five times the amount of energy actually consumed in calendar year 2000. One customer has signed a contract with the Department for interruptible service.

Voluntary Green Power Program. Pursuant to State law, the Department provides residential customers the option of paying additional monthly amounts of \$3, \$7 or \$10 to fund renewable resources. Non-residential customers also can elect to make voluntary payments in amounts ranging from \$8 to \$150 per month. The proceeds of these voluntary payments will be used by the Department to fund the acquisition of energy from renewable resources, such as solar, wind, fuel cells, and landfill gas. See “Power Resources—Purchased Power Arrangements—Other Renewable Resources.” As of January 1, 2003, 3,470 customers had elected to participate in the program.

AVERAGE RATES AND MONTHLY BILLS

	Average Revenue in Cents per kWh				Average Monthly Bills			
	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila
Residential								
500 kWh per month	5.9		6.0	6.2	\$29		\$30	\$31
1,000 kWh per month	7.3	(2)	7.4	7.6	73	(2)	74	76
2,000 kWh per month	8.0		8.1	8.3	159		161	166
Small General Service								
10,000 kWh per month (40kW)	6.1	(2)	6.2	6.4	\$613	(2)	\$624	\$643
Medium General Service								
20,000 kWh per month (60kW)	6.2	6.9	6.4	6.6	\$1,250	\$1,381	\$1,272	\$1,312
200,000 kWh per month (500kW)	6.2	6.8	6.3	6.5	12,395	13,655	12,615	13,015
Large General Service								
400,000 kWh per month (1,000kW)	5.8	6.3	5.9	6.1	\$23,260	\$25,109	\$23,619	\$24,327
1,800,000 kWh per month (5,000kW)	5.8	6.3	5.9	6.1	104,868	113,408	106,486	109,782
High Demand General Service								
6,000,000 kWh per month (20,000kW)	5.6	(3)	(3)	5.9	\$335,642	(3)	(3)	\$356,529
18,000,000 kWh per month (60,000kW)	5.6			5.9	1,006,925			1,069,587

(1) All jurisdictions outside the City of Seattle, except the City of Tukwila.

(2) There are no separate rate schedules for Residential and Small General Service customers located within the network.

(3) All High Demand General Service customers are located in Seattle or Tukwila.

ANNUAL BILL COMPARISONS WITH OTHER PUGET SOUND UTILITIES
(BASED ON RATES IN EFFECT ON APRIL 1, 2003)

Monthly Use		Seattle City Light				Puget Sound Energy (4)	Snohomish County PUD	Tacoma Power
kWh	kW	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila	City of Bellevue	City of Everett	City of Tacoma
Residential								
100		\$87		\$88	\$91	\$128	\$162	\$135
500		352	(2)	358	372	364	493	411
1,000		872		884	911	742	985	757
3,000		2,950		2,986	3,069	2,334	2,956	2,138
Small General Service								
300	1	\$221		\$225	\$231	\$427	\$377	\$325
3,000	10	2,207	(2)	2,246	2,315	2,727	2,790	2,276
12,000	40	8,827		8,986	9,259	10,394	10,831	8,782
Medium General Service								
150,000	500	\$113,100	\$125,280	\$115,080	\$118,680	\$131,604	\$121,546	\$90,425
200,000	500	148,740	163,860	151,380	156,180	162,886	156,721	109,663
360,000	900	267,732	294,948	272,484	281,124	292,901	278,359	196,952
Large General Service								
300,000	1,000	\$210,665	\$228,281	\$213,662	\$220,142	\$228,586	\$219,826	\$180,299
1,000,000	5,000	710,154	778,966	720,949	742,549	864,986	790,647	706,908
2,500,000	7,500	1,751,568	1,893,955	1,776,513	1,830,513	1,831,966	1,802,939	1,444,842
High Demand General Service								
6,000,000	20,000	\$4,027,700			\$4,278,350	\$3,609,265	\$4,396,524	\$3,595,488
18,000,000	60,000	12,083,101	(3)	(3)	12,835,049	10,827,794	13,189,572	10,785,360
24,000,000	60,000	16,018,024			17,022,972	13,734,515	16,891,380	13,093,896
Last Rate Change		4/01/03	4/01/03	4/01/03	5/01/03	2/15/03	10/01/02	3/31/03

(1) All jurisdictions outside the City of Seattle, except the City of Tukwila.

(2) There are no separate rate schedules for Residential and Small General Service customers located within the network.

(3) All High Demand General Service customers are located in Seattle or Tukwila.

(4) For Puget Sound Energy, Large General Service is Primary General Service and High Demand General Service is High Voltage General Service.

Billing and Collection Processes

The Department currently bills its residential customers and some small commercial customers bi-monthly and all other customers monthly. Such bills are due within 15 days of receipt. The Department has established various payment programs for its customers, including a levelized monthly payment program and an electronic funds transfer program. Accounts receivable write-offs by the Department in 2001 and 2002 were less than one percent of energy sales revenue. The Department's collection policy provides for disconnection of power for nonpayment of amounts due the Department, subject to statutory prohibitions against disconnecting customers in winter months.

Financial Policies

The rate covenants in the Department's Parity Bond ordinances do not require the Department to set rates that achieve a specific level of debt service coverage on Parity Bonds. However, the City Council has adopted by resolution financial policies to be used by the Department in setting rates. From 1990 through December 2001, these policies required that rates be set at levels that would be expected to provide debt service coverage of 1.80 times debt service on Parity Bonds. In December 2001 the City Council adopted by resolution new financial policies which require that rates be set at levels that will provide 95 percent confidence that net revenue available to fund capital requirements will be greater than zero, after payment of all operating and maintenance expenses, debt service, City taxes, deposits to the Parity Bond Reserve Fund, and other current obligations. Coverage is expected to exceed 2.0 times debt service on Parity Bonds under the new rate-setting policies. The new policies additionally require that, in the first two years in which they are in effect, rates be set at levels which will allow the accumulation of a \$25 million contingency reserve account. The new rate-setting policies will take effect after the Department has retired all short-term debt obligations, including the 2002 Notes and the amounts borrowed from the Cash Pool, and has accumulated an operating cash balance of \$30 million. Rates will remain at current levels until the new policies take effect, unless increased by the City Council or otherwise changed to pass through increases or decreases in Bonneville rates. See "Power Resources—Purchased Power Arrangements." The Department expects that the conditions which will allow the new financial policies to take effect will be met in mid-2004. See "Historical and Projected Operating Results." The Department's financial policies are subject to change by the City Council.

CUSTOMERS, ENERGY SALES AND PEAK LOADS

Service Area

The Department's 131 square-mile service area consists of the City plus areas extending three to four miles north and south of the city limits. Because of these geographic limitations, the growth of the Department's electric load has resulted exclusively from development within the service area.

Sales to customers located outside the City's boundaries but within the service area represent approximately one-sixth of retail energy sales and revenues. The Department has a franchise agreement with King County that extends until 2007 and franchises with the cities of Shoreline, Burien, Lake Forest Park, SeaTac, and Tukwila that expire between 2015 and 2018. These six jurisdictions represented over 99 percent of the Department's retail energy sales outside the City in 2002. The Department's service area also includes portions of the cities of Normandy Park and Renton.

Largest Customers

The Department's ten largest customers in 2002, in order of their maximum kW demand, were the Boeing Company, Nucor Steel Company (formerly Birmingham Steel Company), the University of Washington, King County, the United States Government, the Jorgensen Forge Corporation, Saint Gobain Containers, the City of Seattle, Seattle Public Schools, and Unico Properties/Union Square Ltd. These customers accounted for approximately 15.2 percent of retail energy sales and 12.9 percent of retail energy revenues in 2002. The load factors of these customers ranged from 6.7 percent to 77.8 percent, with an average load factor of 40.1 percent.

Historical Sales

Energy sales in the Department's service area can be affected by variations in weather conditions. In winter months, colder than normal weather patterns can result in higher loads, due to the extensive use of electricity for heating. However, warmer than normal conditions in summer months do not lead to significant increases in load because of the limited use of residential air conditioning. Temperatures in the service area were near normal in 2000 and 2001. Warmer than normal temperatures in the winter of 2002-2003 have affected sales in 2002 and 2003.

From 1991 through 2000, retail energy sales within the Department's service area increased at an average rate of 0.8 percent per year. In 2001 energy sales were 5.1 percent below the 2000 level. The amount of energy consumed by retail customers in 2001 was influenced by the Department's public appeal for reduced consumption, the price response to a series of substantial rate increases, the local effects of the general economic downturn, and the events of September 11, 2001.

Total sales of energy to residential customers, which constituted 34.0 percent of the Department's energy sales in 2002, were relatively stable over the 1991-2000 period, despite a 1.1 percent average annual increase in the number of customers during this period. The declining level of consumption per customer reflects smaller household size, fuel-switching, the effect of domestic conservation efforts, and enhanced energy efficiency elements of building codes. In 2002, residential consumption was 6.8 percent below the 2000 level.

Commercial and governmental customers accounted for 52.8 percent of total sales in 2002. Sales growth in these customer classes averaged 1.6 percent annually from 1991 to 2000. Consumption by commercial and governmental customers in 2002 was 2.7 percent below the 2000 level.

The industrial customers served by the Department represented 13.1 percent of retail sales in 2002. Sales to this sector exhibited a slight downward trend over the period 1991-2000, declining at an average annual rate of 0.3 percent. In 2002, sales to industrial customers were 13.8 percent lower than in 2000. The local economic recession and the increase in energy prices were major factors in this decline.

A record peak load of 2,059,566 kW was recorded in December 1990 due to unusually cold weather. The 2002 peak load was 1,689,666 kW and occurred in January.

Load Forecast (2003-2008)

The Department's ongoing planning activities include the annual preparation of a forecast of firm system load, derived from a forecasting model that assumes average weather conditions and includes other independent demographic and economic variables developed from an historical service area database. The most recent load forecast presented in the table "Retail Customers, Energy Sales and Energy Requirements" incorporates the estimated impact on load of adopted and projected rate changes, the Department's conservation programs and the residual effects of the Department's efforts to reduce electricity consumption during 2001. See "The Department—Retail Rates."

The forecast of system load for the 2003-2008 period is based on actual experience through April 30, 2003. In 2002, actual load was 0.5 percent above the 2001 level; weather-adjusted load was almost identical to load in 2001. For the first five months of 2003, actual load was 3.7 percent below the level of the corresponding period in 2002, primarily because of warmer than normal weather conditions. Adjusted for weather effects, load was 0.9 percent below the prior year's level. For calendar year 2003, weather-adjusted load is projected to be 0.6 percent below load in 2002. From 2004 through 2008, load is projected to increase at an average annual rate of 1.7 percent.

Both the number of residential customers and sales to the residential sector are expected to increase at an average annual rate of 1.0 percent from 2004 through 2008. Sales to commercial and governmental customers are projected to increase at an average rate of 2.1 percent per year over the same period. As the region emerges from the economic slowdown of 2001-2003, sales to the industrial sector are expected to return to the 2000 level by 2007, implying an annual growth rate of 2.3 percent over the 2004-2008 period. The table below provides a summary of historical and projected customers, energy sales and energy requirements.

RETAIL CUSTOMERS, ENERGY SALES AND ENERGY REQUIREMENTS

	Actual			Projected					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Average Number of Customers ⁽¹⁾									
Residential	316,758	322,707	327,127	332,560	335,556	338,719	341,964	345,347	348,146
Commercial	30,839	30,934	31,418	32,068	32,068	32,068	32,068	32,068	32,068
Governmental	1,686	1,776	1,824	1,829	1,829	1,829	1,829	1,829	1,829
Industrial	276	259	263	258	258	258	258	258	258
Total Customers	349,559	355,676	360,632	366,715	369,711	372,874	376,119	379,502	382,301
Energy Sales (MWh)									
Residential	3,267,710	3,050,900	3,045,768	2,969,717	3,030,320	3,054,684	3,095,944	3,135,293	3,153,164
Commercial	3,932,043	3,829,360	3,872,749	3,724,883	3,816,660	3,843,973	3,917,133	3,992,177	4,065,228
Governmental	908,283	858,111	839,081	857,459	902,482	932,597	976,154	1,022,031	1,061,353
Industrial	1,352,457	1,237,424	1,165,532	1,245,721	1,286,174	1,303,286	1,338,201	1,374,424	1,406,980
Total Energy Sales ⁽²⁾	9,460,493	8,975,795	8,923,130	8,797,780	9,035,636	9,134,540	9,327,432	9,523,925	9,686,725
Peak Demand (MW) ⁽³⁾	1,769	1,662	1,690	2,031	2,094	2,163	2,198	2,198	2,198
Energy Requirements (MWh)									
Total Energy Sales	9,460,493	8,975,795	8,923,130	8,797,780	9,035,636	9,134,540	9,327,432	9,523,925	9,686,725
Energy used in Operation	35,296	32,144	33,672	30,660	30,744	30,660	30,660	30,660	30,744
Energy for Public Lighting ⁽⁴⁾	78,436	78,741	78,859	81,513	82,771	83,514	84,514	85,514	86,784
System Losses ⁽⁵⁾	460,470	392,236	491,005	435,356	447,192	452,059	461,531	471,187	479,210
Total Energy Requirements ⁽⁶⁾	10,034,695	9,478,916	9,526,666	9,345,309	9,596,343	9,700,773	9,904,137	10,111,286	10,283,463

- (1) The Department's forecast projects an increase in the number of residential customers but no change in the number of customers in other classes.
- (2) Energy sales in the Department's service area only.
- (3) Data for 2000, 2001 and 2002 reflect the actual one-hour peak load. Projections for 2003 through 2008 reflect the 16-hour peak load under extremely cold weather conditions.
- (4) Energy for streetlighting in the City of Seattle.
- (5) Includes transmission and distribution losses.
- (6) Firm energy required in the Department's service area.

CHANGE IN THE ELECTRIC UTILITY INDUSTRY

The electric utility industry in the United States has been in a period of change, resulting from actions taken by legislative and regulatory bodies at the national, regional and state levels. The National Energy Policy Act of 1992 (the “Energy Act”) and subsequent orders issued by the Federal Energy Regulatory Commission (“FERC”) require utilities under FERC’s jurisdiction to provide wholesale power suppliers with non-discriminatory, open access to transmission capacity that is surplus to firm retail loads. The result has been greater competition in the wholesale electricity market. Although the Energy Act explicitly prohibited FERC from requiring open access to power suppliers at the retail level (“retail wheeling”), many states have passed legislation or implemented regulations providing for varying degrees of retail wheeling. However, volatility in the wholesale power market in the Western United States in 2000 and 2001 has led some states to significantly modify or rescind existing statutes. In Washington State, legislation to restructure the electric utility industry has not received serious consideration since 1997.

Regional Transmission

In 1999, FERC issued its Order 2000, which set forth certain guidelines and incentives for the formation of Regional Transmission Organizations (“RTOs”). In compliance with FERC Order 2000, Bonneville and nine investor-owned utilities in the Northwest have made various filings with FERC regarding the formation of a regional RTO (“RTO West”) that would assume operational responsibility for transmission facilities in the Pacific Northwest under standardized, FERC-jurisdictional tariffs. The Department depends on contractual arrangements with transmission owners, principally Bonneville, for the transmission of power from Boundary and other generating facilities and for the Department’s wholesale market transactions. The Department therefore would be affected by the establishment of RTO West. The Department has joined other regional utilities in opposing the establishment of RTO West as currently proposed. The Department cannot predict whether efforts to form an RTO will ultimately be successful and, if successful, what the impact will be on the Department’s access to regional transmission facilities and the cost of such access. See “Power Resources—Transmission.”

Standard Market Design

In July 2002, FERC issued a Notice of Proposed Rule-Making (“NOPR”) setting forth standards for the provision of transmission services and the operation of wholesale energy markets in the United States. Under the Standard Market Design (“SMD”) described in the NOPR, transmission services in each region would be provided by an independent transmission provider. Transmission providers would offer a single form of transmission service, Network Access Service, based on an open access tariff. Transmission users would pay an access charge which would be sized to recover the embedded transmission costs of the transmission owners. Parties with existing contracts for transmission services would have the option of converting their contracts to Network Access Service or retaining their rights under the existing contracts. The independent transmission providers would operate both day-ahead and real-time energy markets to manage congestion. Differences between day-ahead and real-time energy prices at many system “nodes” would establish the price for transmission. Load-serving entities would be required to demonstrate that they have access to power resources that are sufficient to meet future retail demand. The SMD also includes provisions for market monitoring and oversight and for independent governance of the transmission providers.

Strong opposition to the proposed SMD has been expressed by state elected officials and regulatory agencies, primarily in the western and southern United States. The Department has stated its opposition to the SMD because, in the opinion of the Department, the uniform standards proposed by FERC takes into account neither the unique features of the Northwest power system, with its heavy dependence on hydroelectric generation, nor the dominance of non-jurisdictional, publicly owned, transmission in the region. Since the release of the July 2002 NOPR, the FERC Chairman has indicated that issuance of a final rule would be deferred until the U.S. Congress has acted on energy policy legislation. FERC has also indicated a willingness to take into account regional differences in its final rule. The Department cannot predict the outcome of the deliberations regarding the SMD or the effects on the Department if the SMD is adopted.

Federal Energy Legislation

Legislation is currently under consideration in the U.S. Congress that would have a significant impact on the energy sector of the U.S. economy. The House of Representatives has passed a bill that, among other things, would expand FERC's jurisdiction over public power organizations, including Bonneville. The Senate Energy Committee has reported a bill that also provides greater FERC jurisdiction over public power systems. However, other features of the Senate bill would limit the ability of FERC to implement standard market design as proposed in the original draft rule. Final action on the Senate bill is expected by late July 2003. A conference committee is likely to be required in order to resolve differences between the House and Senate bills. The Department cannot predict the outcome of the legislative process or the ultimate impact of federal energy legislation on the Department's operations and finances.

RECENT DEVELOPMENTS AFFECTING THE DEPARTMENT

In 2000 and 2001, electric utilities in the western United States, including the Department, were subject to a number of unprecedented developments that had severe negative effects on their financial results. Efforts to restructure the electric utility industry in the State of California created turbulence in wholesale markets for electricity and natural gas. Wholesale prices rose dramatically throughout the western region. At the same time, severe drought conditions in the Northwest required the Department to rely more heavily on the wholesale market in order to meet the demand for electricity. As a result, the Department incurred net costs in excess of \$550 million purchasing power in the wholesale market in 2000 and 2001, more than ten times the amount assumed in its financial plan.

In response to this combination of events, the Department took a number of actions in 2001 and 2002 to deal with the impact of its unexpectedly high power costs.

- (i) The Department requested, and the City Council granted, four separate rate increases in 2001. The cumulative effect of these actions was an increase of 57 percent in average system rates. See "The Department—Retail Rates."
- (ii) The City Council authorized the Department to pass through to its retail customers the financial impacts of changes in power rates charged by Bonneville without further City Council action. The Department's retail rates have been adjusted three times in response to changes in Bonneville rates. See "The Department—Retail Rates" and "Power Resources—Purchased Power Arrangements—The Bonneville Power Administration."
- (iii) The Department increased its target for conservation savings and carried out an intensive public information campaign to encourage customers to reduce their use of electricity. As a result of these efforts and in response to the increase in rates, consumption of electricity by retail customers in the Department's service area fell by 5.1 percent from 2000 to 2001, thereby reducing the need to buy power in the wholesale market.
- (iv) The Department obtained additional sources of power by signing a new contract with Bonneville effective October 1, 2001, and by contracting to purchase power from the Klamath Falls Cogeneration Project and the State Line Wind Project. With over 400 average MW of firm power available from these resources, the Department expects to have surplus power available even under critical water conditions for the next several years.
- (v) In 2002, the Department refinanced \$86.6 million of outstanding Parity Bonds and participated in the refinancing of \$66.1 million of bonds issued by the Boise-Kuna Irrigation District for the Lucky Peak Project. The Department pays all of the costs of the Lucky Peak Project under a purchased power contract and therefore will realize the benefits of the refinancing. Present value savings from these two bond issues totaled over \$10 million.

To finance its operating cash flow requirements in 2000 and 2001, the Department incurred short-term debt. In March 2001 the Department issued \$182.2 million of Revenue Anticipation Notes, which were paid in full at maturity in March 2003. A loan of up to \$110 million from the City's Cash Pool was authorized in

December 2001. In November 2002, the 2002 Notes were issued in the amount of \$125 million. The 2002 Notes will mature in November 2003.

In 2002, with rates at the levels to which they were raised in 2001 and with the return of more normal water conditions to the Northwest, the Department's financial results improved considerably. The Department generated net cash flow from operations of \$97 million in 2002, which was used to reduce its outstanding short-term debt. Favorable financial results have continued in 2003 in spite of water conditions that have not been as favorable as in 2002. The Department has reduced its operating and capital budgets to offset the effect of sub-normal water conditions on cash flow. Through May 31, 2003, the Department has recorded net income of \$26.7 million, compared with \$25.4 million in 2002.

In December 2001, the City Council adopted new financial policies which provide that rates will remain at their current levels (unless increased by the City Council or adjusted to pass through changes in Bonneville rates) until all short-term debt obligations have been repaid and cash balances in the Department's operating account have reached the level of \$30 million. The Department now projects that this point will be reached in the third quarter of 2004. Retail rates can then be set on the basis of new guidelines that give greater recognition to the increased level of risks that the Department faces, given current conditions in power markets. It is anticipated that when the new financial policies take effect in 2005, over 50 percent of the Department's future capital requirements will be financed from operating revenue.

Pending Litigation Before FERC

In two cases currently before FERC, the City is seeking refunds of amounts paid for electricity. Both cases arose from FERC's investigation of the extremely high prices experienced in the California energy markets beginning in May 2000 and continuing into the summer of 2001, which led FERC to issue an order on July 25, 2001 (the "Order").

The Order required a hearing in one case to determine refunds in the California markets operated by the California Independent System Operator and the California Power Exchange. Hearings have been completed and post-hearings briefs submitted. The Order also required a hearing in the second case to determine whether refunds should be ordered for transactions in the Pacific Northwest markets. In September 2001, the administrative law judge issued proposed findings and preliminary recommendations stating that prices in the Northwest were not unreasonable or unjust and refunds should not be ordered. The City filed a brief urging FERC to reject the recommendations and to recognize that the unreasonable prices in California directly affected prices in the Pacific Northwest. Supplemental briefs and evidence were filed by the City and other parties in the wake of Enron's revelation of market manipulation strategies in California. However, on June 25, 2003, FERC issued an order denying refunds in the Pacific Northwest case. The City currently is preparing a motion for rehearing.

The City also is involved in other legal actions relating to the failure of the California Independent System Operator to pay the Department for power deliveries in the fall of 2000. Finally, the City has filed a request to intervene in a FERC investigation of companies that may have cooperated with Enron in transactions designed to adversely affect the California and West Coast markets.

None of these actions is expected to materially adversely affect the financial condition of the Department.

POWER RESOURCES

Overview of Resources

The Department typically meets the majority of its energy requirements from its own power resources. These include four large and three small hydroelectric facilities which generate 7,117,981 MWh of energy, about 49 percent of the energy available to the Department from its owned and contracted resources, under average water conditions. Output from the Department's hydroelectric plants can vary significantly from year to year due to the variability of water conditions. In calendar year 1997, when water conditions were exceptionally good, hydroelectric output totaled 8,346,762 MWh. Under the drought conditions of calendar year 2001,

hydroelectric production fell to 3,941,388 MWh. Water conditions in 2002 were closer to normal, and hydroelectric generation amounted to 6,902,317 MWh, or 47 percent of the total energy available to the Department in that year.

The remainder of the Department's energy requirements are supplied through long-term purchased power contracts and short-term purchases of power in the wholesale market. Purchases of energy from Bonneville provided 31 percent of available energy in 2002, reflecting a substantial increase in purchases from Bonneville under the new power sales contract with Bonneville, which took effect on October 1, 2001. The remaining 22 percent of energy used by the Department in 2002 was provided through long-term contracts with other power providers (16 percent) and through short-term purchases in the wholesale power market (six percent). The average cost of energy available to the Department in 2002 from all sources was \$14.88 per MWh, excluding transmission and depreciation. The average cost of power in calendar year 2003 is projected to be \$14.07 per MWh.

Under the Pacific Northwest Coordination Agreement (the "Coordination Agreement"), the Department and 15 other public and investor-owned utilities in the Northwest have agreed to coordinate the operation of their power generation systems to maximize the firm capability and reliability of the coordinated system. The Coordination Agreement went into effect in 1965 and will terminate on September 24, 2024. Under the terms of the Coordination Agreement, the firm capability of the generating resources of the parties to the agreement is calculated with reference to a critical period, which is defined as the multi-month period of adverse streamflows of historical record during which the amount of firm load that could be served by the firm resources of the parties to the Coordination Agreement was at a minimum. Water conditions would be expected to be better than those of the critical period about 95 percent of the time.

The table below provides an overview of the Department's power resources.

OWNED AND CONTRACTED POWER RESOURCES IN 2004

	One-Hour Peak Capability (MW)	Energy Available Under Critical Water Conditions (MWh) ⁽¹⁾	Energy Available under Average Water Conditions (MWh) ⁽²⁾	Year FERC License Expires
Department-Owned Resources				
Boundary	1,055	2,985,408	4,301,738	2011
Gorge	177	864,612	989,167	2025
Diablo	159	733,212	848,083	2025
Ross	360	657,000	852,947	2025
Newhalem	2	13,613	13,613	2027
Cedar Falls ⁽³⁾	30	47,304	81,833	N/A
South Fork Tolt	17	51,912	51,912	2028
Contract Resources				
Bonneville	1,161 ⁽⁴⁾	4,185,022	4,926,669	N/A
Box Canyon	12	79,056	79,056	2005
Priest Rapids	68	302,424	371,070	2005
Columbia Storage Power Exchange	21	-	-	N/A
Grand Coulee Project Hydro Authority	64 ⁽⁵⁾	236,863	236,863	2022/2027
High Ross	298 ⁽⁶⁾	312,773	312,773	N/A
Lucky Peak	113	249,082	337,322	2030
Metro Cogeneration	1	10,541	10,541	N/A
Klamath Falls	100	744,600	744,600	N/A
State Line Wind Project	50	460,185	460,185	N/A

- (1) Critical water conditions represent the lowest sequence of streamflows experienced in the Northwest region over a historical period of record (1929-1978). The firm energy capability of hydroelectric resources is the amount of energy that would be produced under critical water conditions. Actual water conditions would be expected to be better than critical water conditions about 95 percent of the time.
- (2) Figures in this column represent the average amount of energy that would be produced over all of the water conditions in the period of record (1929-1978).
- (3) The Cedar Falls Hydroelectric Plant is not subject to FERC licensing requirements.
- (4) Approximate. Through purchase of the Slice product, the Department is entitled to 4.6676 percent of the actual output of the Federal System (as defined below under "Purchased Power Arrangements—The Bonneville Power Administration"). The Department is also entitled to purchase 135.6 average MW of Block power (as defined below under "Purchased Power Arrangements—Bonneville Power Administration") from Bonneville in 2004.
- (5) The Department's 50 percent share of installed capacity.
- (6) The Department's contract with the Province of British Columbia provides capacity from November through March in an amount equal to 532 MW minus the actual capacity of the Ross Powerhouse.

Resource Acquisitions

In 1996 the Department completed a Strategic Resources Assessment ("SRA") in which it recommended a strategy of reliance on purchases of power in the wholesale market to fill the gap between loads and resources in the near term. In the first half of 2000 the Department published a Strategic Resource Plan ("SRP") which recommended that the Department pursue a number of alternative power sources and demand-side management options to meet its load requirements beyond 2000. Specifically, the SRP recommended that the Department maximize its purchases of Bonneville power under a new power sales contract that was to take effect on October 1, 2001; purchase as much Bonneville power as possible in the form of the Slice-of-the-System product (the "Slice") (see "Purchased Power Arrangements—The Bonneville Power Administration"); pursue a power sales contract of 100 MW from the Klamath Falls Cogeneration Project to replace power

previously supplied by the Centralia Steam Plant (see “Purchased Power Arrangements—Klamath Falls Cogeneration Project”); increase the level of conservation savings to be acquired through 2010 (see “Conservation”); and acquire additional power from non-hydro renewable resources (see “Purchased Power Arrangements—Wind Generation”). The City Council approved the recommendations of the SRP update, and the Department has acquired the recommended resources.

Resource Capabilities and Costs

The following tables show the actual and projected availability and cost of resources that are in the Department’s current plan to meet its net energy requirements through 2008. Projections for 2003 take into account actual water conditions through May 2003. Precipitation in the watersheds in which the Department’s hydroelectric facilities are located has been about 85 percent of normal in the water year beginning October 1, 2002. As a result, the amount of surplus energy available to the Department in 2003 is now projected to be below normal. Output projected for the years beyond 2003 represent the average output that would be realized over all water conditions experienced in the 1929-1978 period, the period generally used for purposes of regional power planning. The tables contain projections that are based on assumptions about future events. Actual conditions may differ from those assumed, resulting in actual results that vary from those projected.

ENERGY RESOURCES
(MWh)

	Actual			Projected ⁽¹⁾					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Department-Owned Generation									
Boundary	3,809,267	2,339,590	3,971,940	3,443,552	4,301,738	4,290,778	4,282,263	4,291,122	4,302,673
Gorge	959,800	616,754	1,025,291	887,504	989,167	986,045	985,197	985,236	988,704
Diablo	814,712	477,635	900,255	747,494	848,083	845,102	844,453	844,531	847,398
Ross	741,637	392,922	837,204	716,199	852,947	848,744	846,074	848,590	851,681
Cedar Falls/Newhalem	53,780	74,430	89,422	81,643	95,446	95,125	95,125	95,125	95,446
Centralia ⁽²⁾	277,103	0	0	0	0	0	0	0	0
South Fork Tolt	44,090	40,057	78,205	50,669	51,912	51,777	51,777	51,777	51,912
Subtotal	6,700,389	3,941,388	6,902,317	5,927,061	7,139,293	7,117,571	7,104,889	7,116,381	7,137,814
Energy Purchases									
Bonneville ⁽³⁾	1,701,674	2,391,518	4,659,586	4,900,117	4,926,669	4,846,234	5,141,268	5,805,573	5,826,918
Box Canyon	57,746	42,663	43,410	46,858	79,056	45,656	0	0	0
Priest Rapids	363,740	262,188	326,522	311,454	371,070	309,397	45,960	46,000	46,159
CSPE	106,603	102,037	99,348	26,350	0	0	0	0	0
GCPHA	238,987	271,009	248,266	261,786	236,863	236,863	236,863	236,863	236,863
High Ross	296,828	307,738	297,123	296,947	312,773	311,020	309,726	311,474	312,130
Lucky Peak	340,825	188,403	288,848	290,403	337,322	337,233	337,233	337,233	337,322
Metro Cogeneration	7,419	11,915	14,539	14,400	10,541	10,512	10,512	8,760	8,784
Klamath Falls	--	326,104	709,520	655,002	796,780	794,548	383,767	0	0
Wind Resources	--	--	106,493	255,397	460,185	494,014	494,014	494,014	495,367
Seasonal Exchange Received	287,066	395,146	208,538	145,946	109,417	108,604	107,926	108,499	109,496
Wholesale Market Purchases ⁽⁴⁾	2,571,228	2,411,210	898,613	962,872	33,811	64,660	61,691	53,701	62,074
Subtotal	5,972,116	6,709,931	7,900,806	8,167,532	7,674,487	7,558,741	7,128,960	7,402,117	7,435,113
Total Department Resources	12,672,505	10,651,319	14,803,123	14,094,593	14,813,780	14,676,312	14,233,849	14,518,498	14,572,927
Minus Offsetting Energy Sales:									
Firm Energy Sales and Marketing Losses ⁽⁵⁾	249,321	310,670	396,862	195,546	470,765	500,240	525,999	528,582	526,428
Out of System Sales ⁽⁶⁾	96,399	15,956	0	0	0	0	0	0	0
Seasonal Exchange Delivered	269,030	376,950	231,650	127,830	90,846	90,623	90,623	90,329	90,580
Wholesale Market Sales	2,023,060	468,827	4,647,945	4,425,908	4,655,826	4,384,676	3,713,090	3,788,301	3,672,456
Total Net Energy Resources ⁽⁷⁾	10,034,695	9,478,916	9,526,666	9,345,309	9,596,343	9,700,773	9,904,137	10,111,286	10,283,463

Footnotes to Table:

- (1) Projections for 2003 are based on actual water conditions through May 2003. Projections for the 2004-2008 period assume average water conditions.
- (2) The Centralia Steam Plant was sold in May 2000.
- (3) From 1996 through September 30, 2001, the amount of power purchased under the Bonneville contract was limited to 195 average MW. Beginning on October 1, 2001, energy from Bonneville is based on the new Block and Slice Power Sales contract.
- (4) Purchases to compensate for low water conditions and to make up the difference between loads and resources. In 2000 and 2001, the Department's purchases of power in the wholesale market were unusually large, due to poor water conditions.
- (5) Energy provided to Public Utility District No. 1 of Pend Oreille County under Article 49 of the Boundary Project's FERC license and to compensate the PUD for the Boundary Project's encroachment on Box Canyon. From 2002 through 2008, figures on this line also include incremental losses due to expanded activity in the wholesale market.
- (6) Energy delivered to Nordstrom facilities in California.
- (7) Firm energy required in the Department's service area.

COST OF POWER SUPPLY
(\$000)

	Actual			Projected					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Wholesale Market Purchases ⁽¹⁾	\$ 212,402	\$ 518,782	\$ 23,154	\$ 22,287	\$ 973	\$ 1,860	\$ 1,596	\$ 1,673	\$ 2,006
Other Power Purchases:									
Bonneville ⁽²⁾	\$ 34,443	\$ 66,824	\$ 134,805	\$ 158,472	\$ 147,607	\$ 155,187	\$ 170,277	\$ 198,654	\$ 194,019
Box Canyon	998	1,183	1,052	1,042	1,068	633	0	0	0
Priest Rapids	2,136	2,303	2,326	2,551	2,618	2,520	1,734	1,712	1,686
GCPHA	8,406	8,465	7,314	4,206	4,845	2,171	2,225	2,281	2,338
CSPE	0	0	0	0	0	0	0	0	0
High Ross	13,342	13,353	13,358	13,366	13,374	13,385	13,392	13,399	13,406
Lucky Peak	16,985	15,978	12,364	12,661	17,670	17,658	17,712	10,788	4,549
Metro Cogeneration	238	381	1,001	390	390	400	409	419	429
Klamath Falls	0	18,460	39,680	40,713	40,202	42,946	21,662	0	0
State Line Wind Project	0	0	6,474	10,787	18,215	19,631	19,631	19,631	19,685
Int and Ex of Wind Resources	0	0	2,417	5,245	5,346	5,429	5,516	5,604	5,703
Seasonal Exchange Received	6,287	27,964	5,944	4,598	3,546	3,607	3,672	3,778	3,901
Other Services	0	10,094	1,866	5,000	5,120	5,251	5,379	5,510	5,652
BPA Billing Credits ⁽³⁾	(3,531)	(3,713)	(3,067)	(3,740)	(3,705)	(3,668)	(3,520)	(3,479)	(3,429)
Subtotal	\$ 79,305	\$ 161,292	\$ 225,534	\$ 255,293	\$ 256,296	\$ 265,148	\$ 258,087	\$ 258,297	\$ 247,938
Production:									
Centralia ⁽⁴⁾	\$ 7,274	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Hydro Projects ⁽⁵⁾	18,611	17,012	18,546	19,584	20,239	21,109	22,221	22,999	23,655
Control and Dispatch	5,285	6,065	6,282	6,607	6,841	7,010	7,174	7,343	7,525
Subtotal	\$ 31,170	\$ 23,077	\$ 24,829	\$ 26,191	\$ 27,080	\$ 28,118	\$ 29,395	\$ 30,342	\$ 31,180
Total Power Supply Expense	\$ 322,878	\$ 703,151	\$ 273,517	\$ 303,770	\$ 284,349	\$ 295,126	\$ 289,079	\$ 290,312	\$ 281,124
Minus Offsetting Power Revenue:									
Wholesale Power Sales	\$ 103,082	\$ 73,899	\$ 112,796	\$ 150,386	\$ 144,997	\$ 137,230	\$ 116,695	\$ 125,981	\$ 126,561
Other Power Sales ⁽⁶⁾	5,050	41,573	18,995	21,894	27,275	27,028	31,731	32,697	33,257
Net Cost of Power	\$ 214,746	\$ 587,679	\$ 141,727	\$ 131,490	\$ 112,077	\$ 130,869	\$ 140,652	\$ 131,634	\$ 121,306
Total Energy Requirement (MWh)	10,034,695	9,478,916	9,526,666	9,345,309	9,596,343	9,700,773	9,904,137	10,111,286	10,283,463
Average Unit Cost (Dollars/MWh) ⁽⁷⁾	\$ 21.40	\$ 62.00	\$ 14.88	\$ 14.07	\$ 11.68	\$ 13.49	\$ 14.20	\$ 13.02	\$ 11.80

Footnotes to Table:

- (1) Purchases to compensate for low water conditions and to make up the difference between loads and resources. Excludes wheeling costs. In 2000 and 2001, the Department purchased unusually large amounts of power in the wholesale market at high prices due to poor water conditions.
- (2) From 1996 through September 30, 2001, the amount of power purchased under the Bonneville contract was limited to 195 average MW. Beginning on October 1, 2001, the cost of power from Bonneville is based on the new Block and Slice Power Sales contract. The forecast assumes the CRAC adjustments projected by Bonneville. Effective October 1, 2006, Block purchases from Bonneville are assumed to increase by 114.4 MW under the terms of the power sales contract. See “Power Resources—Purchased Power Arrangements—Bonneville Power Administration.”
- (3) Billing credits received from Bonneville for the South Fork Tolt Project.
- (4) The sale of the Centralia Steam Plant was completed in May 2000.
- (5) Includes operation and maintenance costs only.
- (6) Includes conservation and renewal credits under the power sales contract with Bonneville, the recognition of payments from Bonneville for the purchase of conservation savings, revenue from the provision of integration and exchange services related to the State Line Wind Project, revenue related to contracts with Grant County PUD for Priest Rapids power beginning in 2005, the valuation of energy delivered under seasonal exchanges and basis sales, revenue from deliveries of energy to Pend Oreille PUD pursuant to Article 49 of the Boundary Project license, and other energy credits.
- (7) Average cost of power supplied to service area customers after recognizing the net revenue or cost associated with wholesale power sales and purchases.

The Department's Resources

Boundary Hydroelectric Plant. The Boundary Project is located on the Pend Oreille River in northeastern Washington near the Canadian and Idaho borders, approximately 250 miles from Seattle. The plant was placed in service in 1967. It has a one-hour peak capability of 1,055 MW and expected energy output of 4,301,738 MWh in 2004 under average water conditions. The Boundary Project is operated under a Federal Energy Regulatory Commission ("FERC") license which expires on October 1, 2011. The Department plans to apply for renewal of its Boundary license. The most recent FERC-mandated independent safety inspection in August 2000 concluded that the dam facilities were in good condition.

The Boundary Project's FERC license requires that up to 48 MW of the Boundary Project's capacity be assigned, at cost, to Public Utility District No. 1 of Pend Oreille County ("Pend Oreille PUD"). Due to Pend Oreille PUD's increasing loads and other contractual requirements, the amount of Boundary Project power assigned to Pend Oreille PUD is expected to increase from its present 32 MW to the maximum allowable amount of 48 MW in August 2005.

For a discussion of the impacts of fisheries issues on this facility, see "Environmental Matters—Endangered Species Act Issues." Encroachment of British Columbia Hydro and Power Authority's ("B.C. Hydro") Seven Mile Project on the Boundary Project is discussed below under "Ross, Diablo and Gorge Hydroelectric Plants."

Ross, Diablo and Gorge Hydroelectric Plants. The Ross, Diablo and Gorge hydroelectric plants are located on a ten-mile stretch of the Skagit River above Newhalem, Washington, approximately 80 miles northeast of Seattle. Power is delivered to the Department's service area via two double-circuit Department-owned transmission lines. The Ross Plant, located upstream of the other two projects, has a reservoir with usable storage capacity of 1,052,000 acre-feet. Because the Diablo Plant, with usable storage capacity of 50,000 acre-feet, and the Gorge Plant, with usable storage capacity of 6,600 acre-feet, are located downstream from the Ross Dam, their operation is coordinated with water releases from the Ross Reservoir and the three plants are operated as a single system. The combined one-hour peak capability of the three plants is 696 MW. Expected energy output in 2004 under average water conditions is 2,690,197 MWh.

These plants form the Skagit Hydroelectric Project and are licensed as a unit by FERC. FERC-required independent inspections of the Skagit Project in 2002 revealed no deficiencies. In 1995, FERC issued a new 30-year license for operation of the Skagit Project. As a condition of the new license, the Department has taken and will continue to take various mitigating actions relating to fisheries, wildlife, erosion control, archeology, historic preservation, recreation, and visual quality issues.

Although the original plans for the Skagit Project had included raising the height of Ross Dam by 122.5 feet to maximize the hydroelectric potential of the plant, the Canadian province of British Columbia (the "Province") protested on environmental grounds. After a protracted period of litigation and negotiation, an agreement (the "High Ross Agreement") was reached under which the Province agreed to provide the Department with power equivalent to the planned increase in the output of the Ross Plant in lieu of the Department's construction of the addition for 80 years commencing in 1986. The agreement is subject to review by the parties every ten years. The most recent review, concluded in 1998, did not result in any changes to the agreement.

The Department's annual payments to the Province include a fixed charge of \$21.8 million annually through 2020, which represents the estimated debt service costs that would have been incurred had the addition been constructed and financed with bonds. In 2000, the Department began amortizing the remaining annual \$21.8 million payments over the period through 2035. Payment of equivalent maintenance and operation costs and certain other charges began in 1986 and will continue for 80 years. The energy delivered under this agreement in 2004 is expected to amount to 312,773 MWh. One-hour peak capability is 150 MW from April through October; from November through March, one-hour peak capability is equal to 532 MW minus the actual peak capability of the Ross Plant, given actual reservoir elevations behind Ross Dam.

If the Province discontinues power deliveries, the High Ross Agreement provides full authority to the Department to proceed with the originally proposed construction and obligates the Province to return to the Department sufficient funds to permit the Department to increase the height of Ross Dam and make other improvements as originally proposed. This obligation has been guaranteed by the Government of Canada.

As authorized in the High Ross Agreement, B.C. Hydro increased the reservoir elevation of its Seven Mile Project on the Pend Oreille River in the spring of 1988, thereby extending its reservoir across the international border to the tail-race of the Boundary Project. An 80-year contract between the City and B.C. Hydro was signed in 1989 to provide compensation to the Department for the encroachment of Seven Mile Reservoir on the Boundary Project.

Cedar Falls Hydroelectric Plant. The Cedar Falls Hydroelectric Plant (“Cedar Falls”), built in 1905, is located on the Cedar River, approximately 30 miles southeast of Seattle. Cedar Falls was constructed before the adoption of the Federal Water Power Act of 1920 and is not subject to licensing by FERC. Cedar Falls power is delivered through an interconnection with Puget Sound Energy. The one-hour peak capability of the plant is 30 MW. Expected energy generation in 2004 under average water conditions is 81,833 MWh.

Newhalem Hydroelectric Plant. The Newhalem Hydroelectric Plant (“Newhalem”), located on Newhalem Creek, a tributary of the Skagit River, was built in 1921 to supply power for the construction of the Skagit Project. The plant was rebuilt and modernized in 1970. It is operated under a FERC license which expires January 31, 2027. The plant’s power is delivered over Department-owned transmission lines. The one-hour peak capability of the plant is 0.5 MW. Expected energy generation in 2004 under average water conditions is 13,613 MWh.

South Fork Tolt River Hydroelectric Plant. The South Fork Tolt River Hydroelectric Plant (the “Tolt Project”) was placed in commercial operation in 1995. The Tolt Project operates under a 40-year FERC license which expires in 2028. The one-hour peak capability of the installed unit is 16.8 MW. Expected energy production from the Tolt Project is 51,912 MWh. To reduce its cost of power from the Tolt Project, the Department entered into a Billing Credits Generation Agreement with Bonneville in 1993, under which Bonneville makes payments to the Department that have the effect of making the cost of power from the Tolt Project approximately equal to the cost of equivalent power from Bonneville. Payments to the Department under the agreement commenced in 1996 and are expected to amount to \$3.7 million in 2003.

Purchased Power Arrangements

In 2002, the Department purchased approximately 47 percent of its total available system energy from other utilities in the region, including Bonneville, under long-term purchase contracts. Some of these agreements with other utilities provide that the Department is obligated to pay its share of the costs of the generating facilities providing the power, including debt service on bonds issued to finance construction, whether or not it receives any power. The Department has covenanted to treat payment of such costs as part of its purchased power expense and includes such costs in its operating and maintenance expenses.

The Department has in the past and may in the future purchase power under the Western Systems Power Pool Agreement and the Block and Slice Power Sales Agreement described immediately below. Those agreements include an obligation on the part of the Department to post collateral contingent upon the occurrence or nonoccurrence of certain future events within the control of the Department, such as future credit ratings or payment defaults. The Department also has entered, and may in the future enter, into agreements that include an obligation on the part of the Department to make payments or post collateral contingent upon the occurrence or nonoccurrence of certain future events that are beyond the control of the Department, such as future changes in gas prices. Such obligations may be characterized as maintenance and operation charges, and thus would be payable from Gross Revenues of the Light System prior to the payment of debt service.

The Bonneville Power Administration. Bonneville markets power from 30 federal hydroelectric projects, from several non-federally-owned hydroelectric and thermal projects in the Pacific Northwest and from various contractual rights with installed peak generating capacity of 24,080 MW and a firm energy capability of

approximately 8,500 average MW (the “Federal System”). These projects are built and operated by the United States Bureau of Reclamation (the “Bureau”) and the United States Army Corps of Engineers (the “Corps”) and are located primarily in the Columbia River basin. The Federal System currently produces approximately 45 percent of the region’s energy requirements. Bonneville’s transmission system includes over 15,000 circuit miles of transmission lines, provides about 75 percent of the Pacific Northwest’s high-voltage bulk transmission capacity and serves as the main power grid for the Pacific Northwest. Its service area covers over 300,000 square miles and has a population of about ten million. Bonneville sells electric power at cost-based wholesale rates to more than 130 utility, industrial and governmental customers in the Pacific Northwest. Bonneville also sells power directly to eight industrial customers in the region. Bonneville is required by law to give preference to government-owned utilities and to customers in the Northwest region in its wholesale power sales.

A 1982 contract with Bonneville entitled the Department to purchase power from Bonneville in amounts equal to the difference between the Department’s load and the firm generating capability of its owned and contracted resources. Effective August 1, 1996, this contract was amended to limit the amount of power purchased from Bonneville to 195 average MW in each operating year through September 30, 2001. This lower level of purchases from Bonneville was considerably less than the difference between the Department’s load and firm resources. For the remaining term of the contract, the Department filled this gap with purchases of power in the wholesale market.

A Block and Slice Power Sales Agreement with Bonneville covers purchases of power for the ten-year period beginning October 1, 2001. Under the contract, power is delivered in two forms: a shaped block (the “Block”) and a Slice. Through the Block product, power is delivered to the Department in monthly amounts shaped to the Department’s monthly net requirement, defined as the difference between the Department’s projected monthly load and the resources available to serve that load under critical water conditions. The original contract provided for delivery of 163.8 average MW annually as a Block for the period from October 1, 2001, through September 30, 2006, and 278.2 average MW from October 1, 2006, through September 30, 2011. Under the Slice product, the Department receives a fixed 4.6676 percent of the actual output of the Federal System and pays the same percentage of the actual costs of the system. Payments for the Slice product are subject to an annual true-up adjustment to reflect actual costs. True-up payments are made in three equal monthly amounts in the first half of the year following the federal fiscal year to which the payments apply. Power available under the Slice product varies with water conditions, federal generating capabilities and fish and wildlife restoration requirements. Under the most recent estimates of the capability of the Federal System, energy available to the Department through the Slice product is expected to average 426 average MW over all water conditions. Under critical water conditions, the Slice product would provide 334 average MW of energy.

Subsequent to the signing of the Block and Slice contract, the amount of energy to be delivered to the Department by Bonneville has undergone two modifications. In response to Bonneville’s request that its customers temporarily reduce their purchases of power from Bonneville, the Department agreed to a reduction of about 24 average MW in the Slice product for the period from October 1, 2001, through March 31, 2002, and a reduction of about 74 average MW for the period from April 1, 2002, through September 30, 2002. In February 2002 Bonneville agreed to purchase from the Department conservation savings expected to be achieved over the period from October 1, 2001, through September 30, 2003. Conservation savings were estimated at 9.8 average MW for the twelve-month period beginning October 1, 2001, and an additional 9.3 average MW for the subsequent twelve-month period. Bonneville agreed to pay the Department \$27 million for these savings. The amount of energy to be delivered to the Department as a Block was reduced by 9.8 average MW for the period from October 1, 2001, through September 30, 2002, and by 19.1 average MW for the period from October 1, 2002, through September 30, 2011, to recognize the cumulative effect of the conservation savings on the Department’s load. Bonneville has signed a letter of intent in which it has indicated its intention to purchase additional conservation savings in the amount of 7.25 average MW in each of the three federal fiscal years beginning October 1, 2003, 2004 and 2005. The Department’s financial forecast assumes that the amount of energy available through the Block product will be reduced by the amount of the additional conservation savings purchased by Bonneville in each of the three federal fiscal years. As a result of these changes in the amounts of energy to be delivered under the contract, the total amount of power available through the contract under critical water conditions is estimated to be

431.6 average MW for the period from October 1, 2003, through September 30, 2004; 460.9 average MW from October 1, 2004, through September 30, 2006; and 571.6 average MW from October 1, 2006, through September 30, 2011. Under average water conditions, an additional 92 average MW of energy would be available through the Slice product.

In May 2000 Bonneville issued a Record of Decision establishing fees and charges effective October 1, 2001, at levels that were slightly higher than Bonneville's then current rates. The ROD included a Cost Recovery Adjustment Clause ("CRAC") which authorized Bonneville to increase its power rates in order to deal with a number of contingencies that might affect adversely its financial condition.

Increases in Bonneville power rates under the CRAC are authorized under three circumstances. First, a Load-Based CRAC adjustment is authorized to cover the additional cost of purchasing power in the wholesale market to serve increases in demand from Bonneville customers that cannot be accommodated by the Federal System. Second, a Financial-Based CRAC can be imposed if higher than expected market prices cause Bonneville's accumulated net revenues to fall below a threshold level. Finally, a Safety-Net CRAC is authorized in any year in which Bonneville projects that there is a less than 50 percent probability that it will be able to pay all of its financial obligations, including its debt service payments to the U.S. Treasury. The Load-Based CRAC applies to both the Block and the Slice products and can be adjusted at six-month intervals; the Financial-Based CRAC and the Safety-Net CRAC apply only to Block purchases. Bonneville used its authority under the Load-Based CRAC to increase rates by 46 percent, effective October 1, 2001. The Load-Based CRAC adjustment was subsequently changed to 39 percent on April 1, 2002, 32 percent on October 1, 2002, and 39 percent on April 1, 2003. A Financial-Based CRAC adjustment of 11 percent was imposed on October 1, 2002. Bonneville has proposed that a Safety-Net CRAC adjustment be implemented later in 2003. Discussions with Bonneville's customers as to the size of the Safety-Net CRAC adjustment are currently in progress. The Department's financial forecast assumes that a Safety-Net CRAC adjustment of 14 percent will take effect on October 1, 2003.

The Department is required by ordinance to pass through to its customers the effect of changes in Bonneville's rates under the various CRAC provisions. See "The Department—Retail Rates." No further action by the City Council is required to pass through Bonneville CRAC adjustments. The Department passed through the effect of Bonneville's October 1, 2001, Load-Based CRAC adjustment by increasing energy charges for all non-low-income customers by \$0.0055 per kWh, effective October 1, 2001. Bonneville's subsequent rate adjustments have been passed through to the Department's non-low-income customers through a reduction of \$0.0007 per kWh effective April 1, 2002, and an increase of \$0.0008 per kWh effective April 1, 2003. In each instance, rates for low-income customers were increased by one-half of the amount of the increase for other rate classes.

Bonneville has projected that the following Load-Based CRAC adjustments will be required in the period through September 30, 2006:

	<u>Block</u>	<u>Slice</u>
October 1, 2003, through March 31, 2004	21%	22%
April 1, 2004, through September 30, 2004	31	32
October 1, 2004, through March 31, 2005	26	27
April 1, 2005, through September 30, 2005	30	31
October 1, 2005, through March 31, 2006	27	28
April 1, 2006, through September 30, 2006	30	31

The Department's financial forecast assumes that the Load-Based CRAC adjustments projected by Bonneville will take effect. In addition, the Department has assumed that the sum of the Financial-Based CRAC and the Safety-Net CRAC will equal 25 percent from October 1, 2003, through September 30, 2006, and that the Department will be required to make Slice true-up payments to Bonneville in the following amounts:

2004	\$ 5,156,250
2005	11,952,500
2006	15,675,000
2007	13,818,750
2008 through 2011	9,000,000

The Department's forecast of revenue from retail power sales assumes that the effects of Bonneville's CRAC adjustments will be passed through to the Department's non-low-income retail customer classes through a decrease of \$0.0004 per kWh effective from October 31, 2003, through December 31, 2004. The rate reduction for low-income customers is assumed to be \$0.0002 per kWh. Beginning in 2005, when the Department is assumed to set new retail rates pursuant to the financial policies adopted by the City Council in December 2001, the projected costs of the Bonneville contract, including the projected effect of CRAC adjustments, are assumed to be included in the revenue requirements on which rates are based.

While the Department has made the assumptions described above regarding the actual cost and amounts of energy available through the Slice product and the level of Bonneville rates, including the additional charges levied pursuant to the CRAC, each of these factors is subject to uncertainty. Actual prices and quantities may differ from the Department's assumptions. The Department addressed the uncertainties associated with its higher level of Bonneville purchases, and particularly the uncertainties related to the nonfirm component of the Slice product, in its review of financial policies in 2001. See "The Department—Financial Policies."

Energy Northwest (formerly known as the Washington Public Power Supply System). The City is a member of Energy Northwest, a municipal corporation and joint operating agency organized under State law that currently has, as members, ten public utility districts and three municipalities, all located within the State. Energy Northwest has the authority to acquire, construct and operate plants, works and facilities for the generation and transmission of electric power.

Energy Northwest was engaged in the construction of five nuclear generating facilities termed Projects Nos. 1, 2, 3, 4, and 5. Project No. 2 was placed in commercial operation in December 1984 and the other projects were terminated in the 1980s. Pursuant to separate Net Billing Agreements with Energy Northwest and Bonneville with respect to Projects Nos. 1, 2 and 3 (the "Net Billed Projects"), the Department is obligated unconditionally to pay Energy Northwest its pro rata share of the total annual costs of the Net Billed Projects, including debt service. The payments are required to be made whether or not construction is completed, delayed or terminated, or operation is suspended or curtailed. Payment by Bonneville to Energy Northwest of the Department's share of its total annual cost of the Net Billed Projects is made by a crediting arrangement whereby Bonneville credits against amounts that the Department owes Bonneville for the purchase of wholesale power an amount equal to the Department's share of the total annual cost of each Net Billed Project. The agreements provide that the Department purchase from Energy Northwest and, in turn, assign to Bonneville a maximum of 8.605 percent, 7.193 percent and 5.043 percent of the capability of Projects Nos. 1 and 2 and Energy Northwest's ownership share of Project No. 3, respectively. The Department's respective shares may be increased by not more than 25 percent upon default of other public agency participants. To the extent the Department's share of such annual costs exceeds amounts owed by the Department to Bonneville, Bonneville is obligated, after certain assignment procedures, to pay the amount of such excess to the Department as reimbursement or to Energy Northwest directly, but only from funds legally available for that purpose.

Under the Net Billing Agreements, the Department's electric revenue requirements are not affected directly by the cost of completion or termination of the Net Billed Projects, but such revenue requirements may be affected to the extent that the costs of such Projects result in increases in the wholesale power rates of Bonneville. Bonneville has been paying principal of and interest on Project No. 1 revenue bonds since 1980, on Project No. 2 revenue bonds since 1977 and on Project No. 3 revenue bonds since 1982. Bonneville, in

projecting its revenue requirements and wholesale power rates, includes in its estimate the principal of and interest on those bonds issued and projected to be issued and Energy Northwest's operating expenses for the Net Billed Projects.

Klamath Falls Cogeneration Project. An October 2000 agreement with the City of Klamath Falls, Oregon, provides for the purchase of energy and capacity from the Klamath Falls Cogeneration Project, a 500 MW cogeneration facility consisting of a combined-cycle combustion turbine fueled by natural gas. Under the terms of the contract, the Department will receive 100 MW of capacity from the project beginning on July 28, 2001, the project's on-line date, through June 30, 2006, with an option to renew the contract for an additional five years. The Department expects to receive 796,780 MWh of energy from the plant in 2004.

The City of Klamath Falls has contracted with PacifiCorp Power Marketing, Inc. for management of the plant's operations. PPM is also responsible for providing fuel for the plant. Power from the plant is transmitted to the Department's service area over the Department's share of the Third AC Intertie and the Bonneville system. The Department may elect to displace all or a portion of the energy it is entitled to receive from the Klamath Falls Cogeneration Project in any given month. Payment for power consists of a fixed capacity charge and variable charges for the cost of fuel, which will be based on a published index of gas prices in Alberta, Canada, and for operations and maintenance costs. The cost of power under the contract is expected to average approximately \$53 per MWh through June 30, 2006. The actual cost of power may vary from the projected level due to, among other factors, variability in the price of natural gas.

Lucky Peak Hydroelectric Power Plant. The Lucky Peak Hydroelectric Power Plant ("Lucky Peak") was developed by three Idaho irrigation districts and one Oregon irrigation district (the "Districts") and began operation in 1988. Its FERC license expires in 2030. The plant is located on the Boise River, approximately ten miles southeast of Boise, Idaho, at the Lucky Peak Dam and Reservoir. The rated capability of the three generating units at the plant is 101 MW. Energy generation in 2004 under average water conditions is expected to be 337,322 MWh. Since generation is concentrated in the summer months, the plant has no peak capability during the Department's winter peak period.

The Department entered into a 50-year power purchase and sales contract in 1984 with the Districts under which the Department will purchase all energy generated by Lucky Peak, in exchange for payment of costs associated with the plant and royalty payments to the Districts. The Department also signed a transmission services agreement with Idaho Power Company ("Idaho Power") to provide for transmission of power from Lucky Peak to a point of interconnection with the Bonneville system. The Department has contracted to sell the entire net output of the plant for the period from May 1, 2003, through November 30, 2004, at a price equal to the Dow Jones Mid-Columbia Index plus \$3.25 per MWh.

Priest Rapids Hydroelectric Plant. Under an agreement effective through October 2005, the Department receives eight percent of the output of the Priest Rapids Hydroelectric Plant ("Priest Rapids"), owned and operated by Public Utility District No. 2 of Grant County ("Grant PUD"). The Priest Rapids facility has an installed capacity of 855 MW, upgraded from 835 MW by FERC in 1998 due to rewinding of three generators. The Department's share of the development's one-hour peak capacity is 68 MW and its share of output in 2004 under average water conditions is expected to be 371,070 MWh.

In 1995, certain Idaho and Snake River cooperatives filed a complaint with FERC in which they sought entitlement to allocation of power from Priest Rapids under any new license. FERC ruled in 1998 that 70 percent of the project's output would be allocated to the new licensee, with the remaining 30 percent available for purchase pursuant to market-based principles by entities in the broad seven-state Northwest region, while giving certain Idaho cooperatives and the current power purchasers a priority right. FERC also issued an order permitting any entity, not just Grant PUD or another Washington public agency, to file a competing license application. These proceedings could impact the amount of power generated at Priest Rapids and the Department's allocation of power upon expiration of the current contract. See "Environmental Matters—Endangered Species Act Issues."

Contracts executed in March 2002 with Grant PUD provide for the allocation of power and other benefits from the Priest Rapids and Wanapum Projects to the Department over the period from November 1, 2005,

through the end of the new FERC license period for the two projects. Under the terms of these contracts the Department expects to purchase 45,656 MWh of firm and nonfirm power from Grant PUD in calendar year 2006 at a cost of \$347,000. The amount of power available from Grant PUD will decline over time as the PUD's load, and its claim on the projects' output, increases. In addition, in 2006 the Department expects to realize \$3.0 million in net revenue from the sale of the 30 percent share of the projects' output that will be sold pursuant to market-based principles in the seven-state Northwest region under the terms of the FERC order. The Yakama Indian Nation has filed a petition with FERC challenging the new contracts signed by Grant PUD.

Columbia Storage Power Exchange. The Department is one of 41 public and private utilities that, with Bonneville, operated under exchange agreements with the Columbia Storage Power Exchange ("CSPE"). CSPE was responsible for purchasing and marketing Canada's share of the downstream power benefits that resulted from the development of water storage projects in Canada pursuant to a treaty between the U.S. and Canada. The exchange agreements provided for the transfer and assignment of 12.5 percent of such downstream power benefits to the Department and the transfer and assignment thereof, in turn, by the Department to Bonneville. In return, the Department was entitled to specified amounts of energy and capacity from Bonneville. No payments have been required under the agreement since 1998. Power deliveries under the CSPE agreement terminated on March 31, 2003.

Grand Coulee Project Hydroelectric Authority. The Department, in conjunction with the City of Tacoma, Department of Public Utilities, Light Division ("Tacoma"), has power purchase agreements with three Columbia Basin irrigation districts for acquisition of the output from five hydroelectric plants under 40-year contracts expiring between 2022 and 2027. These plants, which utilize water released during the irrigation season, are located along irrigation canals in eastern Washington and have a total installed capacity of approximately 129 MW. The plants generate power only in the summer and thus have no winter peak capability. Plant output and costs are shared equally between the Department and Tacoma. In 2004, under average water conditions, the Department expects to receive 236,863 MWh from the project.

Box Canyon Hydroelectric Plant. The Department purchases power from the Box Canyon Hydroelectric Plant ("Box Canyon") owned and operated by Pend Oreille PUD. The purchase contract, which extends until August 1, 2005, is expected to provide the Department with 79,056 MWh of energy in 2004.

West Point Sewage Treatment Plant Cogeneration. In 1982, the Municipality of Metropolitan Seattle (now part of King County) and the Department executed a contract for the purchase of the electrical output of a cogeneration plant located at the County's West Point Sewage Treatment Plant. The project uses methane gas produced at the treatment plant to provide approximately 1.2 MW of one-hour peak capability from three reciprocating engines. The Department expects to receive 10,541 MWh of energy under the agreement in 2004. The Department is currently discussing with the County various options for changing or extending the current contract, which expires on August 31, 2003.

Wind Generation. An October 2001 agreement with PPM provides for the Department's purchase of energy and associated environmental attributes (such as offsets or emission reduction credits) primarily from the State Line Wind Project in eastern Washington and Oregon. Under the agreement, the Department received wind energy with an aggregate maximum delivery rate of 50 MW per hour from January 1, 2002, through July 31, 2002, and will receive a maximum of 100 MW per hour from August 1, 2002, through December 31, 2021. The Department also expects to receive additional firm energy with an aggregate maximum delivery rate of 25 MW per hour from January 1, 2004, through June 30, 2004, and 50 MW per hour from July 1, 2004, through December 31, 2021, from the State Line Wind Project or other qualifying new wind generation facility. The Department also entered into a ten-year agreement to purchase integration and exchange services from PacifiCorp and a 20-year agreement to sell integration and exchange services to PPM. Energy available from the project is expected to increase from 255,397 MWh in 2003 to 460,185 MWh in 2004.

Exchange with Northern California Power Agency ("NCPA"). The NCPA exchange agreement provides for the Department to deliver 60 MW of capacity and 90,580 MWh of energy to NCPA in the summer. In return, NCPA delivers 46 MW of capacity and 108,696 MWh of energy to the Department in the winter.

Deliveries to NCPA started in 1995 and will continue until the agreement is terminated. Either party has the right to terminate the agreement after May 31, 2014.

Exchange with Tacoma. Since 1963, the Department and Tacoma have coordinated system operations pursuant to an agreement which will remain in effect through October 2003. The agreement provides for the delivery of 37,250 MWh of energy to the Department in August in exchange for the same amount of power in October. Deliveries are shaped uniformly throughout all hours of the respective months. The Department does not expect to renew the agreement when it expires.

Wholesale Market Sales and Purchases

The Department has historically bought and sold energy in wholesale power markets to balance its loads and resources. The amount of energy purchased or sold in the wholesale market has varied with water conditions and with changes in the Department's firm resource base. Prior to 1996, when power available to the Department at critical water levels was roughly equal to its load, the Department typically had surplus power available to sell in the wholesale market when water conditions were above critical levels. With the limitation of its Bonneville purchases in 1996 and the sale of the Centralia Steam Plant in 2000, the Department faced energy deficits at critical water levels, and expected to be a net purchaser of energy in the wholesale market under average water conditions. The Department's new contract with Bonneville, effective October 1, 2001, significantly increased the amount of power available from Bonneville. The acquisition of power from the Klamath Falls Cogeneration Project and the State Line Wind Project further increased the energy resources available to the Department. Demand for power in the Department's service area fell in response to the 2001 rate increases, the Department's encouragement of reduction in usage and the downturn in the local economy. Water conditions were close to normal in the water year beginning October 1, 2001. As a result of all of these factors, the Department had substantial amounts of surplus energy available for sale in the wholesale market in 2002. Sales of surplus power in the wholesale market are expected to continue at high levels over the 2003-2007 period.

The table below displays the actual amounts of energy purchased and sold by the Department in wholesale markets from 2000 through 2002 and the amounts projected to be purchased and sold from 2003 through 2008. In 2000 and 2001, the amount of energy purchased in the wholesale market was substantial due to poor water conditions. The high cost of these purchases reflects high market prices. In 2002, net revenues from wholesale market transactions amounted to \$89.6 million. In 2003, net wholesale revenues are expected to reach \$128.1 million. The net amount of surplus energy available in 2003 is expected to be 7.6 percent below the 2002 level because of less favorable water conditions. However, the effect of low streamflows is expected to be offset by higher market prices. The average price on the Department's wholesale sales is expected to be \$37.08 in 2003, significantly higher than the average price of \$24.27 in 2002. Through June 30, 2003, revenue from sales of surplus energy in the wholesale market, net of wholesale purchases, amounted to \$67.6 million. The Department has secured an additional \$32.1 million of net revenue through forward sales through the end of calendar year 2003. The projection of wholesale market sales and revenue from 2004 through 2007 assumes average water conditions and market prices that average 76 percent of the forward prices for sales at the Mid-Columbia trading hub as of mid-July 2003. Net energy available for sale in the wholesale market is projected to decline from 2004 through 2006 due to load growth in the Department's service area and a reduction in power available under certain existing contracts.

WHOLESALE MARKET SALES AND PURCHASES

	Actual			Projected ⁽¹⁾					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Wholesale Market Purchases (MWh)	2,571,228	2,411,210	898,613	962,872	33,811	64,660	61,691	53,701	62,074
Cost of Purchases (\$000)	\$212,402	\$518,782	\$23,154	\$36,006	\$973	\$1,860	\$1,596	\$1,673	\$2,006
Average Cost (\$/MWh)	\$82.61	\$215.15	\$25.77	\$37.39	\$28.79	\$28.77	\$25.87	\$31.16	\$32.32
Wholesale Market Sales (MWh)	2,023,060	468,827	4,647,945	4,425,908	4,655,826	4,384,676	3,713,090	3,788,301	3,672,456
Revenue from Sales (\$000)	\$103,082	\$73,899	\$112,796	\$164,105	\$144,997	\$137,230	\$116,695	\$125,981	\$126,561
Average Revenue (\$/MWh)	\$50.95	\$157.63	\$24.27	\$37.08	\$31.14	\$31.30	\$31.43	\$33.26	\$34.46
Sales Net of Purchases (MWh)	(548,168)	(1,942,383)	3,749,332	3,463,036	4,622,015	4,320,016	3,651,399	3,734,600	3,610,382
Net Revenue	(\$109,320)	(\$444,883)	\$89,642	\$128,099	\$144,024	\$135,370	\$115,099	\$124,308	\$124,555

(1) Projections for 2003 reflect actual water conditions through May 31, 2003. Projections for the 2004-2008 period assume average water conditions.

Risk Management

The Department's exposure to risk is managed by a Risk Management Committee ("RMC") consisting of the Superintendent, the Deputy Superintendents for Finance and Administration, Power Management and Generation and the Department's Director of Strategic Planning and Risk Manager. The RMC is responsible for managing both market risk and credit risk.

Market Risk. The RMC meets weekly to review and adjust the Department's near-term and long-term strategy for marketing surplus energy or, in periods of deficit, for purchasing energy to meet load. The Department executes trades in the wholesale market to meet load during periods of resource deficit, to dispose of energy that is surplus to the needs of the Department's retail customers and to optimize the value of the Department's hydroelectric resources by purchasing wholesale energy in off-peak hours, when prices generally are low, and selling energy in the peak hours, when prices are generally higher. The Department does not engage in speculative trading in the wholesale market.

Credit Risk. The Department's Credit Committee, which reports to the RMC, consists of the Deputy Superintendent for Power Management and the Department's Finance Director, Director of Customer Accounts and Risk Manager. The Credit Committee meets monthly to manage the credit risk associated with the Department's marketing activities. Finance Division staff review the creditworthiness of counterparties with which the Department trades power in the wholesale market and recommends credit limits for each counterparty. Where appropriate, credit enhancements are recommended for counterparties that do not meet standards of creditworthiness adopted by the Credit Committee. Finance and Power Management staff monitor trading activity to ensure that credit limits established by the Credit Committee are not exceeded and provide status reports to the Credit Committee.

Transmission

Department-Owned Transmission. The Department operates 656 miles of transmission facilities. The principal transmission line transmits power from the Skagit Project to the Department's service area. In 1994, the Department signed an agreement with Bonneville for the acquisition of ownership rights to 160 MW of transmission capability over Bonneville's share of the Third AC Intertie, which connects the Northwest region with California and the Southwest. The benefits from this investment include avoidance of Bonneville's transmission charges associated with power sales and exchanges over the Intertie and the ability to enter into long-term firm contracts with out-of-state utilities. The Oregon Department of Revenue has initiated litigation to collect a property tax on the Department's capacity rights in the Third AC Intertie. The potential liability is about \$500,000 per year. Summary judgment motions were argued in the Oregon Tax Court in May 2003. An appeal to the Oregon Supreme Court is likely to follow the Tax Court's disposition of the case, and an appeal to the United States Supreme Court is possible.

Regional Transmission Organizations. In 1999, FERC issued its Order 2000, which mandated the formation of regional transmission organizations ("RTOs") and set forth various standards for their organization and operation. In response, Bonneville and nine investor-owned utilities in the Pacific Northwest initiated efforts to create "RTO West," a Washington non-profit corporation, to function as the operator of the principal transmission facilities in the Pacific Northwest and provide transmission services under standardized tariffs. The Department cannot predict the ultimate outcome of efforts to establish RTO West or the potential effects on the Department's operations and finances. See "Change in the Electric Utility Industry."

Transmission Arrangements with Bonneville. Contracts with Bonneville provide the Department with 1,962 MW of transmission capacity under a point-to-point ("PTP") transmission service agreement for the period from October 1, 2001, through July 31, 2025. The Department's rights under the current PTP contract are expected to be preserved under RTO West. However, the rates that will apply to services provided by RTO West are uncertain, as are the rates likely to be charged by Bonneville if the formation of RTO West is delayed or abandoned. In its financial forecast, the Department has assumed that wheeling costs will increase by 22 percent from 2004 through 2008.

Power supplied to the Department by B.C. Hydro under the High Ross Agreement is transmitted over Bonneville's lines under a second PTP transmission service agreement extending through 2005. The High

Ross PTP contract was assigned to B.C. Hydro in 1999. B.C. Hydro in turn reassigned the contract to the British Columbia Power Exchange Corporation ("Powerex"). Under the assignment agreement provisions, Powerex pays Bonneville directly for all costs associated with the PTP contract. The Department expects to renew this PTP contract with Bonneville in 2006 for at least an additional ten-year term, and simultaneously to renew the assignment arrangement with B.C. Hydro for the same term. See "Power Resources—The Department's Resources."

Additional purchases of transmission on a nonfirm basis may be required in the future in order to accommodate the Department's sales of power in the wholesale market during the spring runoff.

Other Transmission Contracts. The Department also transmits power under contracts with Idaho Power for the transmission of power from the Lucky Peak Project, with Avista for transmission of power from the Grand Coulee Project Hydroelectric Authority; with Puget Sound Energy for transmission of power from the Cedar Falls and South Fork Tolt Projects, and with other utilities.

Conservation

The Department has pursued a policy of managing as well as meeting energy demand. As a result of the "Energy 1990" study, prepared in 1976, the City decided to pursue conservation as an alternative to participating in Energy Northwest's Projects Nos. 4 and 5. During the 1980s, single-family residential measures dominated the Department's conservation program. Conservation incentive programs in the commercial, industrial and multifamily sectors were added in the 1990s. Because commercial and industrial measures are more cost-effective, the majority of new energy savings acquired in recent years has come from these sectors, a trend that is projected to continue into the future. Since 1977, the Department has achieved almost 100.4 average MW of energy savings through conservation.

The 2000 Strategic Resources Plan called for the Department to accelerate the pace of energy savings through conservation. In the spring of 2001, a work plan was developed which increased the targeted level of energy savings to be achieved annually through conservation programs from six average MW to nine average MW per year. To meet this higher target, the work plan called for the Department to continue to operate its core conservation initiatives for all customer groups while adding some new programs and services to address service gaps.

The new power sales contract with Bonneville that took effect on October 1, 2001, provides a credit of \$0.50 per MWh against the amounts payable under Bonneville's rate schedules for investments in conservation and renewable resources. The Department estimates that this credit will reduce payments to Bonneville by \$2.2 million per year.

Under a March 2002 agreement with Bonneville, Bonneville has paid the Department \$27 million for conservation savings to be achieved over the period from October 1, 2001, through September 30, 2003. As part of this agreement, the Department's purchases of power from Bonneville under the Block product have been reduced by 9.8 average MW from April 1, 2002, through September 30, 2002, and by 19.1 average MW from October 1, 2002, through September 30, 2011. The Department and Bonneville recently signed a letter of intent to execute an amendment to the March 2002 agreement extending funding for another three years. Under the amendment, Bonneville would provide an additional \$24 million of funding to purchase 7.25 average MW per year of conservation savings over the period from October 1, 2003, through September 30, 2006, with concomitant reductions of 7.25 average MW annually in the Department's purchases of Block power from Bonneville.

CAPITAL IMPROVEMENT AND CONSERVATION IMPLEMENTATION PROGRAMS

The Department maintains long-range capital improvement and conservation implementation programs to ensure the availability of adequate supplies of power and to provide a high level of service reliability to its various customer groups. The six-year Capital Improvement Program (“CIP”) for the Department forms a part of the City’s Comprehensive Capital Improvement Program, which is mandated by the State’s Growth Management Act. The City’s biennial budget process determines the annual funding levels for both the CIP and the Conservation Implementation Program.

The Department’s 2003-2008 CIP emphasizes projects that address the long-term performance and reliability of its hydroelectric generation plants, substations and distribution systems. The Department’s Conservation Implementation Program provides funding for investments in the commercial and industrial sectors of the service territory to achieve the Department’s long-term energy savings goal.

The sections below describe the CIP and Conservation Improvement Program that are included in the City’s adopted budget for the 2003-04 Biennium.

Generation

The Department plans to spend \$145.7 million on generation plant improvements over the 2003-2008 period. Expenditures of \$26.3 million are projected to complete the rehabilitation work at the Boundary Project, the Department’s largest and most economical generation resource. This rehabilitation is needed to ensure long-term reliability and to prepare for the FERC relicensing of the Boundary Project when the current license expires in 2011. Expenditures are also planned for the ongoing program of turbine runner replacement at the Boundary Project and at the Ross and Gorge Powerhouses. Mitigation measures required under the terms of the renewed FERC License for the Skagit and Newhalem Projects will require expenditures totaling \$30.8 million over the 2003-2008 period.

Transmission

Over the next six years, the Department expects to spend about \$5.9 million for expansion and replacement of transmission plant.

Substations

Substation expansion and improvements are projected to cost \$50.3 million over the 2003-2008 period. Projects include improvements to protective relaying, circuit breaker replacement, switchgear refurbishment, and transformer replacement. These capital projects are designed to maintain reliability and to increase capacity to provide for load growth.

Distribution

The Department plans to spend \$448.3 million over the 2003-2008 period on improvements and additions to its distribution system. Improvements to the downtown network distribution system, service connections, relocations, and capacity additions account for about 72 percent of these costs. Other projects in this category include the provision of electrical infrastructure related to three local transportation projects, for which the Department expects to be reimbursed for a portion of the cost.

General Plant

Programmed expenditures of \$81.0 million will support general plant projects over the 2003-2008 period. Projects include improvements to the North and South Service Centers and other facilities within the service territory. Investments in information technology, including development of Customer Data Services and Work Process Management Systems, are expected to require expenditures totaling \$45.7 million. Communications improvements, including development of a fiber optic network, advanced radio systems and improved energy management and transmission scheduling, are budgeted at \$11.0 million. Special work equipment, office equipment, replacement of vehicles, and miscellaneous building improvements make up the majority of the remaining costs in the general plant category.

High Ross Payment Amortization

In setting rates for the 2000-2003 period, the City Council directed the Department to amortize the \$21.8 million capital portion of the annual payment to B.C. Hydro under the High Ross Agreement through 2035. (See “Power Resources—The Department’s Resources—Ross, Diablo and Gorge Hydroelectric Plants.”) Each year from 2000 through the final capital payment in 2020, \$9.1 million of the annual payment will be deferred and \$12.7 million will be recognized as an expense. From 2021 through 2035, the deferred costs will be amortized through annual charges of \$12.7 million. The deferred portion of the payments to B.C. Hydro is treated as a component of capital requirements.

Conservation

Capital requirements also include \$143.3 million for the Conservation Implementation Program over the 2003-2008 period. This level of expenditure is expected to enable the Department to meet its annual target for energy savings through 2008. The emphasis of conservation programs in this period will be on the commercial and industrial sectors. See “Power Resources—Conservation.”

Other Potential Capital Projects

The Department continually reviews the need for capital improvements to its distribution and substation infrastructure in order to maintain system reliability and provide for future growth in demand. For example, the City is currently working with a number of real estate developers to develop a long-term plan for mixed-use development in the South Lake Union area, immediately north of the downtown core. If the plan is executed as currently contemplated, the City may incur significant expenditures to provide physical infrastructure for the South Lake Union area, including investments in the electrical distribution system. Adjustments to the Department’s capital improvement program may be required during the forecast period. It is also possible that other projects will be identified in the future that are not included in the Department’s current CIP.

Financing

Capital requirements of \$929.1 million from 2003 through 2008 are expected to be financed through a combination of net revenues from operations, contributions in aid of construction, external funding of conservation programs, the remaining proceeds of the 2001 Parity Bonds, the proceeds of the Bonds, and the proceeds of future Parity Bonds and Subordinate Lien Bonds. In 2003, capital financing will be provided from the remaining proceeds from the 2001 Parity Bonds, contributions in aid of construction, external conservation funding and the proceeds of the Bonds. From 2004 through 2008, net revenue available for capital financing is expected to total \$398.7 million, or 51 percent of capital requirements. The remainder of capital funding in that period is projected to be provided by contributions in aid of construction, reimbursement of costs for transportation-related projects, external conservation funding, and bond proceeds. From 2004 through 2008, Parity Bonds in the amount of \$95.0 million are expected to be issued. Subordinate Lien Bond issuances are projected to be \$120.0 million.

PROPOSED CAPITAL IMPROVEMENT AND CONSERVATION PROGRAMS (2003-2008)
(000s)

	2003	2004	2005	2006	2007	2008	Total
Generation							
Turbine Rehabilitation	\$ 1,992	\$ 7,077	\$ 1,396	\$ 10,128	\$ 7,510	\$ 243	\$ 28,346
Skagit Environmental Mitigation	8,453	1,334	9,268	3,513	4,245	3,992	30,805
Dam Safety	1,285	385	0	0	0	0	1,670
Boundary Rehabilitation Project	8,988	6,481	6,349	2,440	1,773	244	26,275
All Others	6,041	6,155	8,221	7,517	12,215	18,489	58,638
Total Generation	\$ 26,759	\$ 21,432	\$ 25,234	\$ 23,598	\$ 25,743	\$ 22,968	\$ 145,734
Transmission	\$ 923	\$ 949	\$ 962	\$ 986	\$ 1,014	\$ 1,043	\$ 5,877
Substations	\$ 6,887	\$ 8,351	\$ 8,425	\$ 8,630	\$ 8,865	\$ 9,124	\$ 50,282
Distribution							
Network Service Connections and Capacity Additions	\$ 15,524	\$ 15,163	\$ 17,213	\$ 17,567	\$ 18,473	\$ 19,011	\$ 102,951
Non-Network Service Connections	12,153	12,843	11,869	12,159	12,488	12,853	74,365
Non-Network Relocations and Capacity Additions	24,069	24,007	23,812	24,342	25,324	26,063	147,617
26KV Conversion	2,160	2,211	2,621	2,685	2,756	2,835	15,268
Regional Transit	3,951	3,695	10,092	11,978	476	490	30,682
Monorail	341	450	2,117	2,149	818	1,189	7,064
Alaskan Way Viaduct	391	509	7,589	8,533	6,892	6,784	30,698
Street and Floodlights	1,565	1,604	1,553	1,590	1,632	1,681	9,625
All Others	5,088	5,239	4,744	4,860	4,990	5,135	30,056
Total Distribution	\$ 65,242	\$ 65,721	\$ 81,610	\$ 85,863	\$ 73,849	\$ 76,041	\$ 448,326
General Plant							
Service Center Improvements	\$ 142	\$ 185	\$ 619	\$ 634	\$ 650	\$ 667	\$ 2,897
Consolidated Customer Service System	2,819	3,238	0	0	0	0	6,057
Communications Improvements	1,405	1,318	2,029	2,043	2,067	2,123	10,986
Information Technology	7,926	7,481	6,471	7,359	8,064	8,359	45,660
All Others	2,622	2,409	2,776	3,325	2,213	2,058	15,403
Total General Plant	\$ 14,914	\$ 14,632	\$ 11,895	\$ 13,361	\$ 12,994	\$ 13,207	\$ 81,003
Conservation	\$ 20,707	\$ 21,435	\$ 23,479	\$ 24,799	\$ 26,130	\$ 26,748	\$ 143,298
Deferred High Ross Expenses ⁽¹⁾	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 54,620
Total Expenditures All Projects	\$ 144,535	\$ 141,623	\$ 160,708	\$ 166,340	\$ 157,698	\$ 158,234	\$ 929,140
Sources of Funds							
Revenue Available for Capital Projects	\$ 0	\$ 40,239	\$ 86,723	\$ 84,672	\$ 91,803	\$ 95,275	\$ 398,712
Proceeds from Contributions ⁽²⁾	28,441	22,990	34,592	32,375	15,401	23,266	157,064
Decreases/(Increases) in Construction Fund	(23,456)	78,394	(30,092)	(4,937)	934	431	21,273
Proceeds from Parity Bonds	136,445	--	--	55,000	--	40,000	231,445
Proceeds from Subordinate Lien Bonds	--	--	70,000	--	50,000	--	120,000
Costs of Issuance and Discounts/Premiums	3,105	--	(514)	(770)	(440)	(737)	645
Total Funding for Capital Projects	\$ 144,535	\$ 141,623	\$ 160,708	\$ 166,340	\$ 157,698	\$ 158,234	\$ 929,140

(1) In adopting rates for the 2000-2003 period, the City Council directed the Department to amortize the capital portion of annual payments to the Province of British Columbia under the High Ross Agreement over a period extending through 2035. From 2000 until the final capital payment is made in 2020, the \$9.1 million deferred portion of the annual High Ross payment will be included in capital requirements. See "Power Resources—The Department's Resources."

(2) Includes contributions in aid of construction and customer payments for conservation. Also included from 2002 through 2006 are payments received from Bonneville to purchase conservation savings. See "Power Resources—Conservation."

HISTORICAL AND PROJECTED OPERATING RESULTS

In the preparation of the projections in this Official Statement, the City has made certain assumptions with respect to conditions that may occur in the future. While the City believes these assumptions are reasonable for the purpose of the projections, they depend upon future events, and actual conditions may differ from those assumed. The City does not represent or guarantee that actual results will replicate the estimates in the various tables set forth in this Official Statement. The electric industry has undergone significant changes, as discussed in this Official Statement. Potential purchasers of the Bonds should not rely on the projections in this Official Statement as statements of fact. Such projections are subject to change, and will change, from time to time. The City has not committed itself to provide investors with updated forecasts or projections.

Neither the Department's independent auditors, nor any other independent accountants, have compiled, examined or performed any procedures with respect to the projected financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and assume no responsibility for, and disclaim any association with, the prospective financial information.

Historical Results—2000-2002

Financial results in 2000 and 2001 were heavily influenced by water conditions in the Northwest region and by price levels in the wholesale power market. Energy available to the Department in 2000 and 2001 had been reduced by the sale of the Centralia Steam Plant in May 2000 and by extremely poor water conditions in the water year beginning October 1, 2000. At the same time, wholesale market prices increased to extremely high levels. In 2000, the Department's purchases of power in the wholesale market exceeded its sales by 548,168 MWh. The net cost of wholesale transactions was \$109.3 million. In 2001, net purchases amounted to 1,942,383 MWh at a net cost of \$444.9 million.

Revenues from sales of electricity to retail customers in the Department's service area rose from \$383.7 million in 2000 to \$500.9 million in 2001 and \$562.4 million in 2002. The 46.6 percent increase in retail revenue from 2000 to 2002 reflects the four rate increases implemented in 2001. See "The Department—Retail Rates." Offsetting the effect of the rate increases, the volume of sales fell by 5.1 percent from 2000 to 2001 and by an additional 0.6 percent in 2002. See "Customers, Energy Sales and Peak Loads."

The cost of power supply, including wholesale market purchases, long-term purchased power contracts and the operating costs of the Department's hydroelectric facilities, increased from \$322.9 million in 2000 to \$703.2 million in 2001. The cost of wholesale market purchases increased from \$212.4 million in 2000 to \$518.8 million in 2001, as a result of poor water conditions and high market prices in 2001. With water conditions and market prices at more normal levels in 2002, the cost of wholesale purchases fell to \$23.2 million. Purchased power costs increased from \$79.3 million in 2000 to \$161.3 million in 2001 and \$225.5 million in 2002 as additional power became available under the Department's contracts with Bonneville, the City of Klamath Falls and the State Line Wind Project. The cost of Bonneville power increased from \$34.4 million in 2000 to \$66.8 million in 2001 and \$134.8 million in 2002. Power from the Klamath Falls Cogeneration Project cost \$18.5 million in 2001 and \$39.7 million in 2002. Delivery of power from the State Line Wind Project commenced in 2002 at a cost of \$6.5 million.

Wheeling costs increased from \$18.4 million in 2000 to \$21.9 million in 2001 and \$31.1 million in 2002. A 25 percent increase in Bonneville's transmission rates on October 1, 2001, was the main cause of the growth in wheeling costs. Other operating and maintenance costs for transmission, distribution, customer services, conservation, and administration rose from \$104.6 million in 2000 to \$115.6 million in 2001 and \$119.3 million in 2002. Some of the growth in costs from 2000 to 2001 reflected the fact that expenses in 2000 were offset by payments for services. In 2001 and 2002 these payments were treated as operating revenues, rather than as offsets to expense.

Debt service payments on Parity Bonds decreased from \$83.2 million in 2000 to \$61.6 million in 2001, reflecting the refinancing of certain scheduled payments of principal and interest in 2001 and the capitalization of \$9.8 million in interest costs on the 2001 Parity Bonds. Principal and interest payments on the

Department's \$503.7 million 2001 Parity Bond issue caused debt service in 2002 to increase to \$110.7 million.

Debt service on Subordinate Lien Bonds decreased from \$6.7 million in 2000 to \$5.7 million in 2001 and \$4.9 million in 2002 as short-term interest rates fell to low levels.

In 2000, net revenue available for debt service was equal to 1.26 times debt service on Parity Bonds and 1.16 times debt service on Parity Bonds and Subordinate Lien Bonds. In 2001, the City Council authorized the deferral of \$300 million in excess power costs from 2001 to the following three years. The Department will amortize the deferred costs in equal monthly amounts from January 2002 through December 2004. With net revenue in 2001 calculated to include the deferred power costs, net revenue was equal to 1.42 times debt service on Parity Bonds and 1.30 times debt service on Parity Bonds and Subordinate Lien Bonds. In 2002, net revenue was equal to 1.61 times Parity Bond debt service and 1.54 times Parity Bond and Subordinate Lien Bond debt service. If net revenue is adjusted to exclude the amortization of \$100 million of power costs deferred from 2001, Parity Bond debt service in 2002 would be covered 2.51 times.

Projected Results—2003

The Department currently projects retail revenues of \$551.4 million in 2003, a reduction of \$11.0 million, or 2.0 percent, from the prior year. The volume of energy sales is projected to be 1.4 percent lower than in 2002, due to continuing weakness in the local economy and warmer weather in the 2002-2003 winter.

Revenue from wholesale sales is projected to be \$164.1 million. With wholesale purchases at a projected level of \$36.0 million, net revenue from wholesale transactions is expected to be \$128.1 million, a significant improvement over the \$89.6 million in net wholesale revenue recorded in 2002. Through mid-June 2003, power worth \$99.7 million had either been delivered to other counterparties or sold forward for delivery by the end of the year. Higher prices in the wholesale market account for most of the growth in wholesale revenue. The average price for wholesale sales in 2003 is expected to be \$37.08 per MWh. In 2002 the average sales price was \$24.27 per MWh. The amount of power delivered in the wholesale market, net of wholesale purchases, is expected to be 7.6 percent lower in 2003 than in 2002, due to less favorable water conditions in 2003.

Purchased power costs are projected to increase from \$225.5 million in 2002 to \$255.3 million in 2003. The cost of power purchased from Bonneville is expected to be \$158.5 million in 2003, an increase of \$23.7 million from 2002. True-up payments for the Slice product and a projected 14 percent Safety-Net CRAC increase effective October 1, 2003, account for most of this increase. Purchases of power from the State Line Wind Project are also projected to increase, raising costs by \$4.3 million.

Operation and maintenance expenses, excluding wholesale purchases, purchased power costs and taxes, are expected to increase by \$1.1 million from 2002 to 2003, an increase of 0.7 percent. A projected reduction in wheeling costs of \$0.9 million partially offsets an increase of \$1.4 million in operations and maintenance costs at the Department's hydroelectric plants. Costs in the remaining categories of operations and maintenance are projected to increase by \$0.7 million.

Parity Bond debt service is projected to be \$105.7 million in 2003, a decrease of \$5.0 million from the 2002 level, reflecting the retirement of Parity Bonds at maturity and the refinancing of bonds in December 2002. Debt service on Subordinate Lien Bonds is projected to increase from \$4.9 million in 2002 to \$5.3 million in 2003, due primarily to an increase in scheduled maturities.

Net revenue available for debt service in 2003, before taking into account the amortization of power costs deferred from 2001, is projected to be \$275.3 million, which is sufficient to cover Parity Bond debt service 2.60 times and the sum of Parity Bond and Subordinate Lien Bond debt service 2.48 times. When the amortization of \$100 million of deferred power costs is recognized, Parity Bond debt service is projected to be covered 1.66 times. Parity Bond and Subordinate Lien Bond debt service is expected to be covered 1.58 times.

Through May 31, 2003, the Department recorded net income of \$26.7 million, an increase of \$1.4 million from the same period in 2002. A decrease in retail revenues was offset by an increase in net revenue from wholesale market sales and purchases and a reduction in purchased power costs. Operations and maintenance costs, excluding hydroelectric production, purchased power and wheeling, increased by \$2.9 million from the prior year. Interest expense was \$3.8 million lower, and contributions in aid of construction increased by \$2.2 million.

STATEMENT OF REVENUES, EXPENSES AND NET INCOME
JANUARY 1 THROUGH MAY 31
(\$000, UNAUDITED)

	<u>Actual</u>		<u>Increase/</u>
	<u>2003</u>	<u>2002</u>	<u>(Decrease)</u>
Operating Revenues			
Retail Power Revenues	249,792	265,343	(15,551)
Wholesale Power Revenues	79,742	52,169	27,573
Other Revenues	5,662	4,696	966
Total Operating Revenues	335,196	322,208	12,988
Operating Expenses			
Operation and Maintenance Expense *	230,944	212,377	18,567
Taxes	27,700	28,655	(955)
Depreciation	29,049	29,197	(148)
Total Operating Expenses	287,693	270,229	17,464
Net Operating Income:	47,503	51,979	(4,476)
Nonoperating Revenues/(Expenses)			
Investment Income	3,075	4,187	(1,112)
Other Income (Expense), Net	(100)	49	(149)
Interest Expense	(31,129)	(34,949)	3,820
Amortization of Debt Expense	(496)	(1,186)	690
Total Nonoperating Revenues/(Expenses)	(28,650)	(31,899)	3,249
Income/(Loss) before Contributions, Grants, and Transfers	18,853	20,080	(1,227)
Contributions, Grants and Transfers			
Contributions in Aid of Construction	7,515	5,318	2,197
Grants and Transfers	367	(49)	416
Total Contributions, Grants and Transfers	7,882	5,269	2,613
NET INCOME/(LOSS)	26,735	25,349	1,386

* In December 2001, \$300 million of short-term power purchases incurred in 2001 were deferred and are being amortized at \$100 million annually in 2002, 2003 and 2004. For 2002 and 2003, year-to-date purchased power costs include the amortization of \$41.7 million of purchased power costs deferred from 2001.

Projected Results—2004-2008

The Department's current forecast of retail revenue assumes that average rates in 2004 will be 1.4 percent higher than in 2003 due to the increase in rates effective May 1, 2003, for customers in the City of Tukwila and an increase in the rates to be paid by the Department's sole interruptible customer in 2004. Average rates are expected to fall by 3.7 percent in 2005 when new rates are expected to take effect pursuant to the Department's new financial policies. The new financial policies require that rates in 2005 and 2006 be sufficient to provide 95 percent confidence that net revenues after payment of all current obligations will be at least \$12.5 million in each year in order to fund a contingency reserve account of \$25 million. In 2008, with the contingency reserve account fully funded, rates are assumed to be 5.2 percent below the 2005 level. See "The Department—Financial Policies."

The forecast of wholesale market sales and purchases assumes average water conditions throughout the 2004-2008 period. Net revenue from wholesale market transactions is expected to range from a high of \$144.0 million in 2004 to a low of \$115.1 million in 2006. The amount of surplus energy available for sale in the wholesale market is projected to decline from 2004 through 2006, as the energy available from a number of contracted resources declines and as system load increases. In 2007, an increase in the amount of energy available under the Bonneville power sales contract, effective October 1, 2006, is assumed to be partially offset by the expiration of the contract for power from the Klamath Falls Cogeneration Project. The average price for wholesale sales is expected to rise from \$31.14 per MWh in 2004 to \$34.46 per MWh in 2008. The prices assumed in the 2004-2008 period are substantially lower than current prices in the forward market for that period, which exceed \$40 per MWh. See "Power Resources—Wholesale Market Sales and Purchases."

Purchased power costs are projected to be relatively stable from 2004 through 2008, ranging from a high of \$265.1 million in 2005 to a low of \$247.9 million in 2008. The expiration of the Klamath Falls contract is the major factor contributing to the decline in purchased power costs from 2005 through 2008.

Wheeling costs are projected to increase from \$34.4 million in 2004 to \$41.8 million in 2008, due to projected increases in transmission rates.

Other costs of operations and maintenance are projected to increase from \$123.3 million in 2004 to \$141.2 million in 2008. Conservation costs, including the cost of amortizing the Department's growing conservation investments, are expected to increase throughout the period, from \$11.8 million in 2004 to \$16.1 million in 2008. Excluding conservation, operations and maintenance costs are projected to increase at an average rate that exceeds the rate of inflation by one percent.

Financing the Department's capital requirements is expected to require the issuance of \$95 million of Parity Bonds and \$120 million of Subordinate Lien Bonds over the period from 2004 through 2008. In these years, approximately 51 percent of capital requirements are expected to be financed from current revenues, with the remainder of the financing coming from bond proceeds (32 percent) and contributions in aid of construction and payments from Bonneville and customers for conservation programs (17 percent).

Debt service on Parity Bonds is projected to increase from \$122.6 million in 2004 to \$129.2 million in 2008. Debt service on Subordinate Lien Bonds is expected to rise from \$6.9 million in 2004 to \$16.3 million in 2008. Before recognizing the amortization of deferred power costs, coverage in 2004 is expected to be 2.48 times debt service on Parity Bonds and 2.35 times the sum of Parity and Subordinate Lien Bonds debt service. If the amortization of deferred power costs is taken into account, coverage in 2004 is expected to be 1.67 times Parity Bonds debt service and 1.58 times total debt service. Over the 2005-2008 period, net revenues are expected to be equal to 2.16 times debt service on Parity Bonds and 1.96 times total debt service.

Uncertainty of Projections and Potential Mitigating Actions

In projecting its financial results for the period through 2008, the Department has made a number of assumptions regarding the factors that affect its financial performance. If actual experience differs from the assumptions made with regard to these factors, the Department's actual financial results could differ significantly from the results projected in its forecast. The factors the Department believes are most likely to

affect its financial results are load growth within the Department's service territory, water conditions in the watersheds of concern to the Department, prices in the wholesale power market, and prices charged by Bonneville under its power sales contract with the Department.

Load Growth. If load growth in a given year were to exceed the amount projected, the amount of surplus energy available to the Department would be reduced. The Department would receive more revenue from sales to its retail customers and less revenue from sales of surplus energy in the wholesale market. Through 2008 the Department's average revenue per MWh of retail sales (net of taxes) is projected to be higher than the average price in the wholesale market. Under these conditions, an increase in load would result in a net financial benefit to the Department. For example, if load in 2004 were one percent higher than projected, the net benefit to the Department would be about \$2.4 million, given the assumptions in the forecast regarding the Department's rates and prices in the wholesale market. Conversely, if load were one percent lower than projected, the Department's net revenue would be about \$2.4 million lower than projected. The effect of load variances is expected to diminish in the years beyond 2003 because the difference between the Department's average retail rate and the average market price is projected to narrow.

Water Conditions. The Department expects to have an average of approximately 4.0 million MWh of surplus energy available for sale in the wholesale market over the 2004-2008 period under average water conditions. Under adverse water conditions that would be expected to be exceeded with 95 percent confidence, the amount of surplus energy available could be as low as 1.4 million MWh in a given year. With water in short supply, wholesale market prices might be expected to be higher than normal. Under these circumstances, revenues from surplus energy sales would therefore be approximately \$70 million lower than currently projected. Conversely, under favorable water conditions that would be expected to be exceeded with five percent confidence, the amount of surplus energy available could be as high as 7.0 million MWh. Under such surplus conditions, market prices would be expected to be lower than normal, and revenues from the sale of the surplus would be approximately \$50 million higher than projected.

Wholesale Market Prices. The Department expects to sell its surplus energy in the wholesale market at average prices ranging from \$31.14 per MWh in 2004 to \$34.46 per MWh in 2008. Wholesale market prices in the Department's forecast from 2004 through 2007 are about 24 percent lower than forward prices in the wholesale market as of mid-July 2003. The price projected for 2008 is the 2007 price plus inflation. If the actual price in the wholesale market in a given year exceeds these estimates by \$1 per MWh and the amount of surplus energy available is at the expected level of approximately 4 million MWh, the Department would realize approximately \$4 million in additional revenue. Conversely, the Department's revenues would be reduced by \$4 million if the wholesale market price were \$1 per MWh below the price assumed in the forecast.

Bonneville Prices. The prices charged by Bonneville under its power sales contract with the Department currently include surcharges of 49.5 percent on the Block product and 39.5 percent on the Slice product under the CRAC. The Department is required by City ordinance to pass through the effects of changes in the Bonneville surcharge on its costs by adjusting retail rates. If the Bonneville surcharge for both the Block and Slice products were to increase by ten percentage points in a given year, the Department's purchased power costs would increase by about \$12 million, and retail rates would increase by approximately two percent to offset the resulting increase in costs. Conversely, if the surcharge were to decline by ten percentage points, the Department would experience a \$12 million reduction in its costs, and retail rates would be lowered by about two percent. Therefore, any increases or decreases in Bonneville rates would result in increases or decreases in the Department's retail rates, but would not affect net revenue.

Mitigating Actions. If actual results differ from those assumed in the Department's projections due to the risk factors discussed above, the City has a number of options for dealing with the financial consequences. First, the Department could take action to reduce its operating costs. Second, the City could leave rates in effect at their current levels for a longer period of time than now anticipated, deferring the point in time at which the new financial policies would allow rates to be reduced. Third, the City could increase rates beyond their current levels. Fourth, the City could mitigate any cash flow problems through the use of temporary loans from the City's Cash Pool. Finally, the City could issue additional short-term debt instruments.

SUMMARY OF HISTORICAL AND PROJECTED OPERATING RESULTS ⁽¹⁾
(\$000)

	Actual			Projected					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Operating Revenues:									
Retail Energy Sales in Seattle Service Area ⁽²⁾									
Residential	\$ 150,773	\$ 187,802	\$ 210,221	\$ 203,052	\$ 206,354	\$ 202,112	\$ 209,957	\$ 202,344	\$ 197,849
Commercial	152,085	206,083	239,964	230,405	236,062	228,159	237,991	231,094	229,047
Governmental	33,585	43,958	50,655	51,351	54,060	53,477	57,272	57,250	57,850
Industrial	47,231	63,043	61,592	66,589	77,447	74,949	78,645	77,006	76,729
Subtotal	\$383,674	\$500,886	\$562,432	\$551,397	\$573,924	\$558,697	\$583,865	\$567,694	\$561,476
Retail Energy Sales Outside Service Area ⁽³⁾	7,904	2,551	0	0	0	0	0	0	0
Wholesale Power Sales	103,082	73,899	112,796	164,105	144,997	137,230	116,695	125,981	126,561
Power Exchanges and Other ⁽⁴⁾	5,050	41,573	18,995	21,894	27,275	27,028	31,731	32,697	33,257
Transmission Revenues ⁽⁵⁾	2,138	2,731	2,116	2,532	2,216	2,272	2,328	2,384	2,446
Other Revenue	3,781	7,922	12,992	12,799	12,944	12,753	13,130	13,522	13,868
Total Revenue	\$505,629	\$629,562	\$709,330	752,728	\$761,356	\$737,980	\$747,750	\$742,278	\$737,608
Operating Expenses Before Debt Service:									
Wholesale Market Purchases	\$ 212,402	\$ 518,782	\$ 23,154	\$ 36,006	\$ 973	\$ 1,860	\$ 1,596	\$ 1,673	\$ 2,006
Long-Term Purchased Power Contracts	79,305	161,292	225,534	255,293	256,296	265,148	258,087	258,297	247,938
Production	31,170	23,077	24,829	26,191	27,080	28,118	29,395	30,342	31,180
Wheeling	18,432	21,906	31,065	30,126	34,367	35,769	38,103	38,937	41,846
Other Operating and Maintenance Expenses ⁽⁶⁾	104,555	115,603	119,333	120,055	123,327	128,422	133,023	137,296	141,245
Taxes (excluding City taxes)	18,845	21,915	26,256	27,014	28,072	28,112	29,097	28,229	28,455
Total Operating Expenses Before Debt Service	\$ 464,709	\$ 862,575	\$ 450,171	\$ 494,684	\$ 470,115	\$ 487,429	\$ 489,301	\$ 494,773	\$ 492,669
Net Operating Revenue	\$40,920	(\$233,013)	\$259,159	\$258,044	\$291,242	\$250,551	\$258,449	\$247,505	\$244,938
Add:									
Amortization Included in Operating Expenses ⁽⁶⁾	\$ 7,825	\$ 8,873	\$ 9,803	\$ 7,434	\$ 6,311	\$ 7,540	\$ 8,957	\$ 10,031	\$ 11,085
Proceeds of Property Sales ⁽⁷⁾	41,464	(8)	695	2,000	2,000	2,051	2,101	2,152	2,208
Operating Fees and Grants	565	1,382	741	300	300	300	300	300	300
Other Income	13,868	10,370	7,428	7,547	6,632	11,387	12,090	12,796	12,998
Revenue Available for Debt Service	\$ 104,642	\$ (212,396)	\$ 277,825	\$ 275,325	\$ 306,485	\$ 271,829	\$ 281,897	\$ 272,784	\$ 271,530

Footnotes to Table:

- (1) Results for 2001 have been restated to comply with recent changes in accounting standards. Several items that are included in revenues in the table above had been treated as offsets to operating expenses prior to the restatements.
- (2) The projection of revenue from retail sales reflects the average rate increase of 1.2 percent that took effect on April 1, 2003, and the increase in rates for customers in the City of Tukwila that took effect on May 1, 2003, and assumes a reduction of 0.4 percent effective October 1, 2003, to pass through anticipated changes in Bonneville rates. Beginning in 2005, rates are assumed to be set in compliance with the new financial policies established by the City Council. Average rates are assumed to decline by 3.7 percent in 2005 and by an additional 5.2 percent from 2005 to 2008. See “The Department—Financial Policies.”
- (3) Sales to Nordstrom facilities in California.
- (4) Includes conservation and renewal credits under the power sales contract with Bonneville, the recognition of payments from Bonneville for the purchase of conservation savings, revenue from the provision of integration and exchange services related to the State Line Wind Project, revenue related to contracts with Grant County PUD for Priest Rapids power beginning in 2005, the valuation of energy delivered under seasonal exchanges, revenue from deliveries of energy to Pend Oreille PUD pursuant to Article 49 of the Boundary Project license, and other energy credits.
- (5) Includes revenue from the rental of transmission facilities to Bonneville and Snohomish County PUD and revenue from the sale of transmission capacity.
- (6) Includes certain non-cash amortization expenses. Non-cash expenses are not taken into account in determining the amount of net revenue available for debt service. Net revenues therefore are adjusted to exclude these costs
- (7) Proceeds from the sale of the Centralia Steam Plant in 2000 amounted to \$41,399,000.

HISTORICAL AND PROJECTED DEBT SERVICE COVERAGE
(\$000)

	Actual			Projected					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Revenue Available for Debt Service	\$ 104,642	\$ (212,396)	\$ 277,825	\$ 275,325	\$ 306,485	\$ 271,829	\$ 281,897	\$ 272,784	\$ 271,530
Deferral/(Amortization) of Power Costs ⁽¹⁾		300,000	(100,000)	(100,000)	(100,000)				
Adjusted Revenue Available for Debt Service	\$ 104,642	\$ 87,604	\$ 177,825	\$ 175,325	\$ 206,485	\$ 271,829	\$ 281,897	\$ 272,784	\$ 271,530
Debt Service:									
Parity Bonds	83,206	61,552	110,665	105,719	123,373	124,332	125,478	129,762	129,765
Subordinate Lien Bonds	6,680	5,749	4,870	5,304	6,947	10,260	12,377	13,230	16,285
Total Debt Service	\$ 89,886	\$ 67,301	\$ 115,535	\$ 111,024	\$ 130,320	\$ 134,592	\$ 137,855	\$ 142,992	\$ 146,050
Debt Service Ratios (giving effect to deferral/amortization of power costs) :									
Times Covered - Parity Bonds ⁽²⁾	1.26	1.42	1.61	1.66	1.67	2.19	2.25	2.10	2.09
Times Covered - Parity and Subordinate Lien Bonds ⁽³⁾	1.16	1.30	1.54	1.58	1.58	2.02	2.04	1.91	1.86
Debt Service Ratios (without giving effect to deferral/amortization of power costs) :									
Times Covered - Parity Bonds ⁽⁴⁾	1.26	(3.45)	2.51	2.60	2.48	2.19	2.25	2.10	2.09
Times Covered - Parity and Subordinate Lien Bonds ⁽⁵⁾	1.16	(3.16)	2.40	2.48	2.35	2.02	2.04	1.91	1.86

- (1) Deferral of excess power costs in 2001 and amortization of these costs in 2002, 2003 and 2004 has been authorized by the City Council.
- (2) Determined by dividing Adjusted Revenue Available for Debt Service by Parity Bond Debt Service.
- (3) Determined by dividing Adjusted Revenue Available for Debt Service by the sum of Parity Bond Debt Service and Subordinate Lien Bond Debt Service.
- (4) Determined by dividing Revenue Available for Debt Service by Parity Bond Debt Service.
- (5) Determined by dividing Revenue Available for Debt Service by the sum of Parity Debt Service and Subordinate Lien Bond Debt Service.

ENVIRONMENTAL MATTERS

Impact of Environmental Matters

Environmental responsibility and stewardship are identified as corporate values in the Department's strategic and business planning efforts. The Department manages its legal obligations for environmental protection through programs that are expected to produce compliance with regulations. Although the Department cannot predict the outcome or effect of the matters described in this section, the Department does not expect that any of these matters will affect adversely its ability to pay the principal of and interest on the Bonds.

Waste Management and Disposal Issues

Routine operations in connection with the generation and delivery of electric power are regulated by federal, state and local laws that prescribe standards, work practices and training requirements and require extensive documentation to ensure the protection of the environment and human health. Noncompliance creates the potential for violations that can result in civil and criminal penalties and substantial fines. Some of these laws also impose strict liability for environmentally damaging releases, including costs of investigation and cleanup, damages, restoration, and the costs of agency oversight and enforcement.

Department operations generate a variety of wastes including hazardous wastes. However, the Department's efforts have reduced hazardous waste generation and disposal costs and the Department maintains those reduced levels. The Department promotes compliance with federal and State hazardous waste regulations through use of operations manuals, staff training and periodic internal inspections or audits. During internal audits, compliance with other laws, including the Toxic Substances Control Act, Clean Water Act and Underground Storage Tank regulations, is monitored.

Through the Department's pollution prevention programs, more than six million pounds of oil contaminated with polychlorinated biphenyls ("PCBs") has been removed from the system and pesticide use has been substantially reduced. Additionally, pollution prevention efforts have resulted in annual reductions of 26,000 pounds of oil-, solvent- and paint-contaminated water, 3,000 pounds of contaminated shop towels and 800 pounds of solvents.

Contaminated Site Liability

In 2001, the EPA listed the Lower Duwamish Waterway as a Superfund site. In anticipation of this listing, the City (through the Department and Seattle Public Utilities), King County, the Port of Seattle, and the Boeing Company entered into a voluntary administrative consent order with the EPA and the State Department of Ecology to perform a remedial investigation and feasibility study ("RI/FS") along the Lower Duwamish Waterway. The Department has recorded a \$2.5 million environmental liability as of December 31, 2002, for its share of actual and estimated future costs associated with the RI/FS. This amount will be evaluated annually and is subject to adjustment based on future developments. It is likely that the Department will be liable for a portion of the costs of future remediation of the Lower Duwamish site. The Department will be liable for some costs of remediation of an area known as Slip 4, due to the Department's ownership and operation of the Georgetown Steam Plant, which was decommissioned in 1980. The City is taking the lead role in further investigation of contamination at Slip 4. A preliminary estimate of the total cost of investigating and remediating Slip 4 sediments is \$8 million to \$10 million. The Department also will be liable for some of the costs of remediating sediments in an area known as Terminal 117, adjacent to a former asphalt plant. The Port of Seattle has taken the lead role in further investigation of Terminal 117. An estimate is not yet available for the cost of remediation of Terminal 117. The Department expects to share the costs of investigating and remediating contamination of Slip 4 and Terminal 117 with other responsible parties; however, the extent of such sharing or later recovery of costs is not known at this time. The Boeing Company has discovered PCB contamination on its Plant II property, some of which Boeing attributes to a substation operated by the Department. The Department has investigated and believes it is unlikely that the PCBs came from the substation; however, work to determine the source and the extent of the contamination is ongoing. If the substation is determined to be a source of the contamination, then the Department may be liable for some of the costs of investigation and remediation.

No assurances can be given that other contaminated sites do not exist or will not be discovered in the future. The Department's policy has been to undertake voluntary cleanup action when contamination is discovered during maintenance and construction.

Endangered Species Act Issues

A number of fish species inhabit the waters where hydroelectric projects are owned by the Department, or from which the Department purchases power. Some species have been, or may be in the future, listed under the Endangered Species Act ("ESA") as either "threatened" or "endangered." The overall long-run implications of these listings are difficult to assess. Two legal mechanisms that typically come into play and that could affect project operation are the Section 7 "consultation" requirement and the Section 9 "take" prohibition. Where an activity that may affect a listed species has a federal "nexus"—that is, where an activity is undertaken, permitted or funded by a federal agency—that agency is required to consult with either the National Oceanic and Atmospheric Administration ("NOAA Fisheries," formerly the National Marine Fisheries Service) for salmon and steelhead or the U.S. Fish and Wildlife Service ("USFWS") for other species, such as bull trout. The purpose of the consultation is to ensure that the activity will not "jeopardize" the continued existence of the species or adversely modify its critical habitat. Biological Opinions are prepared, in appropriate cases, and mandatory conditions may be placed on the conduct of the activity or project in order to avoid causing jeopardy. A FERC decision to issue a hydroelectric project license, or license amendment, has a nexus with ESA and triggers Section 7 consultation.

Columbia and Snake River Anadromous Fish Issues. There are three federal "action agencies" responsible for the operation of the Federal System: the Corps, the Bureau and Bonneville. These agencies have been engaged in consultation for a number of years, and NOAA Fisheries has been required as a result of litigation to develop a series of Biological Opinions relating to the Columbia and Snake River fisheries. In 1995, NOAA Fisheries developed a broad species recovery plan, including recommendations for upstream and downstream passage requirements. These requirements include minimum flow targets for the entire Columbia Basin designed to maximize the survival of downstream migrating juvenile salmon and steelhead and upstream migrating adult salmon and steelhead. In May 1998 and December 2000, NOAA Fisheries and USFWS developed supplemental plans that identify reasonable and prudent alternatives to protect and recover not only listed salmon and steelhead but also bull trout and sturgeon that have been listed under the ESA in the Columbia River Basin.

The Department's power generation at its Boundary Project has been affected by the recovery plans and the Biological Opinions on which they were based. Specifically, the Biological Opinions require reservoirs upstream from the Boundary Project to store more water during the winter for release in the spring and summer when it is needed for downstream juvenile fish migration. Generation at the Boundary Project therefore is reduced in the fall and winter, when the region experiences its highest sustained energy demand. Due to the recommendations of the Biological Opinions, the water not released in the fall and winter on the Pend Oreille River is released in the spring and summer, when it is sometimes spilled because the Boundary Project does not have sufficient hydraulic capacity to use all the available water for generation. This results in a reduction in the Boundary Project's firm capability under the terms of the Pacific Northwest Coordination Agreement ("PNCA"), a system-wide contract for coordinating power generation among federal and other generating utilities in the region. Other Department-owned projects can also be affected by the PNCA, but not as directly as the Boundary Project. The Department does have a contract with Grant County PUD No. 1 to obtain eight percent of the output from the Priest Rapids Project and a contract with Bonneville to receive 4.6676 percent of output from the Federal System. The Biological Opinions may have similar effects on the amounts the Department receives under these contracts. It is unknown at present how new Biological Opinions to support recovery plans will affect power generation capabilities at the Boundary Project. In the opinion of the Department, it is possible that new opinions will result in some changes in flows that could have an impact on the Boundary Project.

Other Endangered Species Issues. Other fish listings that may affect Department operations include bull trout and chinook salmon in Puget Sound. Bull trout have a wide geographic range in the Pacific Northwest, and sub-populations are present in most of the reservoirs and rivers used for hydroelectric generation, including all three reservoirs of the Skagit Project. The Skagit populations are generally recognized as being among the

healthiest in the State due to excellent habitat conditions, cold water temperatures and an abundant food supply. Bull trout are also found in the Cedar Falls Hydroelectric Project reservoir. Studies currently are under way to determine the status of the populations and any potential impacts of the hydroelectric projects on bull trout downstream of the Skagit Project and in its reservoirs. The studies will be used to develop management plans in cooperation with State and federal agencies.

Listed chinook salmon are present in the Skagit, Tolt and Cedar Rivers downstream of hydroelectric facilities on those rivers. The hydroelectric facilities are above natural passage barriers in the case of the Skagit and Tolt Rivers. While it is unclear how these listings might affect operations, the Department may be able to minimize adverse impacts on its operations for a number of reasons. On the Cedar River, the Department's activities are covered by a Habitat Conservation Plan that authorizes operations with regard to all listed species of the Cedar Falls Hydroelectric Project and by an incidental take permit. Both the Skagit and South Fork Tolt River projects were licensed through a collaborative process involving State and federal regulatory agencies, including NOAA Fisheries and USFWS, and tribes. These agreements include extensive measures to protect fish, including complex flow controls and non-flow measures such as habitat restoration and research and monitoring. In addition, the Department is carrying out an ESA Early Action program that will assist in the recovery of chinook and bull trout and address any further impacts related to these issues.

Clean Water Act Issues

Section 401 of the federal Clean Water Act requires states to provide a "water quality certification" regarding compliance of discharges with State water quality requirements as a precondition for federal actions including licensing of hydroelectric projects. The purpose of the certification is to ensure that the project complies with State water quality standards. These standards address various physical and chemical parameters, and Section 401 also has been interpreted to authorize states to condition their certification on maintenance of a minimum stream flow determined to be necessary to protect fish.

An agreement with State and federal agencies was reached on minimum flows for the Newhalem Creek plant, and incorporated into the FERC license issued in 1997. These minimum flows were a condition of the Section 401 certification issued in 1996. The license for the Boundary project expires in 2011 and the Department is currently preparing for the relicensing process. Water quality studies at the Boundary Project are currently underway in support of that process. It is unknown to what extent these issues may affect power generation capability pursuant to a new license.

Renewable Energy and Carbon Dioxide Mitigation

The City Council has passed resolutions committing the Department to acquire new renewable resources, setting a goal of meeting the electric energy needs of the City with no net greenhouse gas emissions. In response, the Department has signed a contract to acquire greenhouse gas offsets (i.e., a reduction in greenhouse gas emissions at one location to compensate for emissions at another location) and has purchased output and associated environmental attributes from the State Line Wind Project in eastern Washington and Oregon. See "Power Resources—Purchased Power Arrangements—Wind Generation." Finally, the Department is offering customers the opportunity to contribute to the acquisition of additional renewable resources, as required by State law. See "The Department—Retail Rates." Customer contributions initially will be used to install solar electricity systems on public facilities, with an emphasis on schools. The Department is currently evaluating additional renewable energy options to pursue with this funding.

Electromagnetic Fields

Many studies have been conducted regarding potential health effects resulting from exposure to power line frequency electric and magnetic fields ("EMF"). A 1999 report to Congress of the National Institute of Environmental Health Sciences ("NIEHS") concluded that the scientific evidence that power frequency EMF poses health risk is weak. The report recommended that because some, albeit weak, evidence suggests there may be some health concerns, there should be a focus on "passive" actions aimed at exposure reduction. The Department has a policy of evaluating ways to minimize EMF in the design and construction of new utility facilities, and provides information and measurements for customers and employees. Since publication of the

1999 NIEHS report, there have not been significant research developments that have changed the NIEHS conclusions.

THE CITY OF SEATTLE

The following provides general information about the City.

Municipal Government

Incorporated in 1869, the City of Seattle, Washington, is the largest city in the Pacific Northwest and is the county seat of King County (the “County”). The City’s elected officials are a mayor, nine City Council members and a city attorney. These officials are elected at large to four-year terms. The City provides four utility services funded by rates and charges: electricity, water, drainage and wastewater, and solid waste.

Financial Management

City financial management functions are provided by the Department of Finance. Dwight D. Dively is the Director of Finance. Mr. Dively is a graduate of Rose-Hulman Institute of Technology, holds a master’s degree from Princeton University in public affairs and is a Ph.C. in civil engineering at the University of Washington.

Accounting. The accounting and reporting policies of the City conform to generally accepted accounting principles for municipal governments and are regulated by the State Auditor’s Office, Division of Municipal Corporations, which maintains a resident staff at the City to perform a continual current audit as well as the annual post-fiscal year audit of City financial operations. The Department of Finance maintains general supervision over financial transactions of all City funds. In addition, the City’s utilities are audited annually by an external auditor.

Auditing. The State Auditor is required to examine the affairs of all local governments at least once every three years; the City is audited annually. The examination must include, among other things, the financial condition and resources of the City, compliance with the laws and Constitution of the State, and the methods and accuracy of the accounts and reports of the City. Reports of the Auditor’s examinations are required to be filed in the office of the State Auditor and in the Department of Finance. The City’s Comprehensive Annual Financial Report may be obtained from the Department of Finance by calling (206) 684-8300.

Municipal Budget. City operations are guided by a budget prepared under the direction of the Mayor by the City Budget Office within the Department of Finance pursuant to State statute (Chapter 35.32A RCW). The proposed budget is submitted to the City Council by the Mayor each year not later than 90 days prior to the beginning of the next fiscal year. Currently the fiscal year of the City is from January 1 through December 31. The City Council considers the proposed budget, holds public hearings on its contents and may alter and revise the budget at its discretion, subject to the State requirement that budgeted revenues must at least equal expenditures. The City Council is required to adopt the budget at least 30 days before the beginning of the next fiscal year.

Investments. **The information in this section does not pertain to pension funds, which are administered by the Seattle City Employees’ Retirement System, and some debt issuance proceeds that are administered by trustee service providers.**

All cash-related transactions for the City, including its utilities, are administered by the Treasury Division of the Department of Finance. City cash is deposited into a single bank account and cash expenditures are paid from a consolidated disbursement account. Investments of temporarily idle cash may be made, according to existing City Council-approved policies, by the Treasury Division in the following securities:

- (i) U.S. Treasury and agency issues;
- (ii) bankers’ acceptances sold on the secondary market;

- (iii) repurchase and reverse repurchase agreements, when structured with securities eligible for purchase and when executed under an approved Master Repurchase Agreement with selected primary dealers; and
- (iv) commercial paper purchased in the secondary market which has received the highest ratings of at least two nationally recognized rating agencies.

State statutes, City ordinances and Department of Finance policies require the City to minimize market risks by safekeeping all purchased securities according to governmental standards for public institutions and by maintaining safety and liquidity above consideration for returns. Current City investment policies require periodic reporting about the City's investment portfolio to the Mayor and the City Council. The City's investment operations are reviewed by the City Auditor and by the State Examiner.

As of May 31, 2003, the combined investment portfolios of the City totaled \$847.8 million at book value. The City's cash pool is constituted solely of City funds. The City does not invest any of its funds in other pools, with the exception of tax collection receipts initially held by the County and funds of the Seattle City Employees' Retirement System and the Deferred Compensation Plan. The year-to-date yield on the City's consolidated pool of investments as of May 31, 2003, was 3.4 percent. As of May 31, 2003, the average maturity date of the portfolio was January 7, 2005. Approximately 37.1 percent, or \$314.9 million, was invested in securities with maturities of three months or less. The City held no securities with maturities longer than 15 years. Investments were allocated as follows:

U.S. Treasury Securities	53.7%
Commercial Paper	23.7
Municipal Investment Account	8.8
Federal Farm Credit Bank	7.2
Repurchase Agreements	3.5
Federal Discount Notes	2.5
Certificates of Deposit	0.4

Interfund Loans. City ordinances authorize the Director of Finance to approve interfund loans for a duration of up to 90 days and to establish a rate of interest on such loans. Extension or renewal of interfund loans requires City Council approval by ordinance. The Director of Finance also is authorized by City ordinance to make loans to individual funds participating in a common investment portfolio by carrying funds in a negative cash position for a period of up to 90 days, or for a longer period upon approval by ordinance, to the extent that such loans can be supported prudently by the common investment portfolio and the borrowing fund is reasonably expected to be able to repay the loan. Loans of this type bear interest at the common investment portfolio's rate of return.

Risk Management

The City maintains \$25 million liability insurance, with a \$5 million self-insured retention per occurrence. The City also maintains \$500 million policy limits of property insurance, with a \$500,000 deductible per occurrence and other underlying limits and deductibles. However, damage to City utility property is not insured, except for certain property used for administrative purposes. Workers compensation is self-insured. Miscellaneous other policies are purchased to cover other exposures such as fiduciary and crime liability.

Pension System

Nearly all permanent non-uniformed City employees participate in the Seattle City Employees' Retirement System (the "Plan"), a single employer public employee retirement system. The payroll for City employees covered by the Plan for the year ended December 31, 2001, was \$405.0 million; total City payroll was \$619.5 million. Nearly all City employees are required to contribute 8.03 percent of their annual base salary to the Plan, and the City contributes an additional 8.03 percent. As of January 1, 2001, system assets exceeded the accrued actuarial liability. The actuarial present value of future benefits was \$1.988 billion, the actuarial present value of future normal costs for present members was \$497.8 million and the actuarial value of assets available for benefits was \$1.493 billion. Combined employee and employer contributions to the

Plan totaled approximately \$69.3 million for the year ending December 31, 2001. Due to declining investment returns, the system's unfunded liability as of January 1, 2003, has increased significantly.

Labor Relations

The City has 34 separate departments and offices with approximately 13,000 regular and temporary employees. Thirty different unions and 45 bargaining units represent approximately 75 percent of the City's regular employees. The City's contract with the Seattle Police Officers Guild expired on December 31, 2002, and negotiations for a successor contract are underway. The parties are using an "interest-based" approach rather than traditional positional bargaining. The contract with the Seattle Police Management Association (representing lieutenants and captains in the Police Department) expired at the end of 2001, and negotiations for a successor contract are continuing. The City is currently in the middle of three-year contracts with the coalition of City unions representing most non-uniformed City employees, and with IBEW Local 77, which represents electrical workers in the City Light and Transportation departments. The City also has agreements with Firefighters Local 27 and Fire Chiefs Local 2898 that generally extend through 2004.

INITIATIVE AND REFERENDUM

Under the State Constitution, Washington voters may initiate legislation and require the Legislature to refer legislation to the voters through the powers of initiative and referendum, respectively. Any such law approved by a majority of the voters may not be amended or repealed by the Legislature within a period of two years following enactment, except by a vote of two-thirds of all the members elected to each house of the Legislature. After two years, the law is subject to amendment or repeal by the Legislature in the same manner as other laws. The Washington State Constitution may not be amended by initiative.

The three most recent State-wide tax-related initiatives approved by State voters did not purport to affect utility rates or charges, though earlier voter-passed initiatives, which were invalidated by the State courts, might have affected utility rates or charges. Other tax and fee initiative measures have been and may be filed, but it cannot be predicted whether any such initiatives might gain sufficient signatures to qualify for submission to the Legislature and/or the voters or, if submitted, whether they ultimately would become law.

Under the City Charter, Seattle voters also may initiate local legislation and City Charter amendments and through referendum may prevent legislation passed by the City Council from becoming law.

LEGAL AND TAX INFORMATION

Bond Litigation

There is no litigation pending with process properly served on the City questioning the validity of the Bonds or the power and authority of the City to issue the Bonds.

Approval of Counsel

Legal matters incident to the authorization, issuance and sale of the Bonds by the City are subject to the approving legal opinion of Foster Pepper & Shefelman PLLC, Bond Counsel. A form of the opinion of such firm with respect to the Bonds is attached hereto as Appendix B. Bond Counsel will be compensated only upon the issuance and sale of the Bonds.

Tax Exemption

Exclusion from Gross Income. In the opinion of Bond Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issue date of the Bonds, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals.

Continuing Requirements. The City is required to comply with certain requirements of the Code after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Note proceeds and the facilities financed or refinanced with Note proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances, and the arbitrage rebate requirement to the extent applicable to the Bonds. The City has covenanted in the Bond Ordinance to comply with those requirements, but if the City fails to comply with those requirements, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds.

Corporate Alternative Minimum Tax. While interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, under Section 55 of the Code, tax-exempt interest, including interest on the Bonds, received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations (as defined for federal income tax purposes). Under the Code, alternative minimum taxable income of a corporation will be increased by 75 percent of the excess of the corporation's adjusted current earnings (including any tax-exempt interest) over the corporation's alternative minimum taxable income determined without regard to such increase. A corporation's alternative minimum taxable income, so computed, that is in excess of an exemption of \$40,000, which exemption will be reduced (but not below zero) by 25 percent of the amount by which the corporation's alternative minimum taxable income exceeds \$150,000, is then subject to a 20 percent minimum tax.

For taxable years beginning after December 31, 1997, the corporate alternative minimum tax is repealed for a small business corporation that had average gross receipts of less than \$5 million for the three-year period beginning after December 31, 1994, and such a small business corporation will continue to be exempt from the corporate alternative minimum tax so long as its average gross receipts do not exceed \$7.5 million.

Tax on Certain Passive Investment Income of S Corporations. Under Section 1375 of the Code, certain excess net passive investment income, including interest on the Bonds, received by an S corporation (a corporation treated as a partnership for most federal tax purposes) that has Subchapter C earnings and profits at the close of the taxable year may be subject to federal income taxation at the highest rate applicable to corporations if more than 25 percent of the gross receipts of such S corporation is passive investment income.

Foreign Branch Profits Tax. Interest on the Bonds may be subject to the foreign branch profits tax imposed by Section 884 of the Code when the Bonds are owned by, and effectively connected with a trade or business of, a United States branch of a foreign corporation.

Certain Other Federal Tax Consequences

Bonds Not "Qualified Tax-Exempt Obligations" for Financial Institutions. Section 265 of the Code provides that 100 percent of any interest expense incurred by banks and other financial institutions for interest allocable to tax-exempt obligations acquired after August 7, 1986, will be disallowed as a tax deduction. However, if the tax-exempt obligations are obligations other than private activity bonds, are issued by a governmental unit that, together with all entities subordinate to it, does not reasonably anticipate issuing more than \$10,000,000 of tax-exempt obligations (other than private activity bonds and other obligations not required to be included in such calculation) in the current calendar year, and are designated by the governmental unit as "qualified tax-exempt obligations," only 20 percent of any interest expense deduction allocable to those obligations will be disallowed.

The City is a governmental unit that, together with all subordinate entities, reasonably anticipates issuing more than \$10,000,000 of tax-exempt obligations (other than private activity bonds and other obligations not required to be included in such calculation) during the current calendar year and has not designated the Bonds as "qualified tax-exempt obligations" for purposes of the 80 percent financial institution interest expense deduction. Therefore, no interest expense of a financial institution allocable to the Bonds is deductible for federal income tax purposes.

Reduction of Loss Reserve Deductions for Property and Casualty Insurance Companies. Under Section 832 of the Code, interest on the Bonds received by property and casualty insurance companies will reduce tax deductions for loss reserves otherwise available to such companies by an amount equal to 15 percent of tax-exempt interest received during the taxable year.

Effect on Certain Social Security and Retirement Benefits. Section 86 of the Code requires recipients of certain Social Security and certain Railroad Retirement benefits to take receipts or accruals of interest on the Bonds into account in determining gross income.

Other Possible Federal Tax Consequences. Receipt of interest on the Bonds may have other federal tax consequences as to which prospective purchasers of the Bonds may wish to consult their own tax advisors.

Original Issue Premium. The Bonds maturing on November 1 in the years 2004 through 2022, inclusive, have been sold at prices reflecting original issue premium ("Premium Bonds"). An amount equal to the excess of the purchase price of a Premium Bond over its stated redemption price at maturity constitutes premium on such Premium Bond. A purchaser of a Premium Bond must amortize any premium over such Premium Bond's term using constant yield principles, based on the purchaser's yield to maturity. The amount of amortizable premium allocable to an interest accrual period for a Premium Bond will offset a like amount of qualified stated interest on such Premium Bond allocable to that accrual period, and may affect the calculation of alternative minimum tax liability described above. As premium is amortized, the purchaser's basis in such Premium Bond is reduced by a corresponding amount, resulting in an increase in the gain (or decrease in the loss) to be recognized for federal income tax purposes upon a sale or disposition of such Premium Bond prior to its maturity. Even though the purchaser's basis is reduced, no federal income tax deduction is allowed. Purchasers of Premium Bonds, whether at the time of initial issuance or subsequent thereto, should consult with their own tax advisors with respect to the determination and treatment of premium for federal income tax purposes and with respect to state and local tax consequences of owning such Premium Bonds.

Original Issue Discount. The Bonds maturing on November 1 in the years 2023 through 2025, inclusive, and the Term Bonds maturing on November 1, 2028, have been sold at prices reflecting original issue discount ("Discount Bonds"). Under existing law, the original issue discount in the selling price of each Discount Bond, to the extent properly allocable to each owner of such Discount Bond, is excluded from gross income for federal income tax purposes with respect to such owner. The original issue discount is the excess of the stated redemption price at maturity of such Discount Bond over the initial offering price to the public, excluding underwriters and other intermediaries, at which price a substantial amount of the Discount Bonds of such maturity were sold.

Under Section 1288 of the Code, original issue discount on tax-exempt bonds accrues on a compound basis. The amount of original issue discount that accrues to an owner of a Discount Bond during any accrual period generally equals (i) the issue price of such Discount Bond plus the amount of original issue discount accrued in all prior accrual periods, multiplied by (ii) the yield to maturity of such Discount Bond (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period), less (iii) any interest payable on such Discount Bond during such accrual period. The amount of original issue discount so accrued in a particular accrual period will be considered to be received ratably on each day of the accrual period, will be excluded from gross income for federal income tax purposes, and will increase the owner's tax basis in such Discount Bond. Any gain realized by an owner from a sale, exchange, payment, or redemption of a Discount Bond will be treated as gain from the sale or exchange of such Discount Bond.

The portion of original issue discount that accrues in each year to an owner of a Discount Bond may result in certain collateral federal income tax consequences. The accrual of such portion of the original issue discount will be included in the calculation of alternative minimum tax liability as described above, and may result in an alternative minimum tax liability even though the owner of such Discount Bond will not receive a corresponding cash payment until a later year.

Owners who purchase Discount Bonds in the initial public offering but at a price different from the first offering price at which a substantial amount of those Discount Bonds were sold to the public, or who do not purchase Discount Bonds in the initial public offering, should consult their own tax advisors with respect to the tax consequences of the ownership of such Discount Bonds. Owners of Discount Bonds who sell or otherwise dispose of such Discount Bonds prior to maturity should consult their own tax advisors with respect to the amount of original issue discount accrued over the period such Discount Bonds have been held and the amount of taxable gain or loss to be recognized upon that sale or other disposition of Discount Bonds. Owners of Discount Bonds also should consult their own tax advisors with respect to state and local tax consequences of owning such Discount Bonds.

Continuing Disclosure Undertaking

Undertaking to Provide Notice of Material Events. To meet the requirements of United States Securities and Exchange Commission (“SEC”) Rule 15c2-12(b)(5) (the “Rule”), the City will undertake in the Bond Resolution (the “Undertaking”) for the benefit of holders of the Bonds, as follows.

Annual Financial Information. The City agrees to provide or cause to be provided to each nationally recognized municipal securities information repository designated by the SEC in accordance with the Rule (each “NRMSIR”) and to a state information depository, if one is established in the State of Washington and recognized by the SEC (the “SID”), annual financial information and operating data regarding the Light System of the type included in this Official Statement as generally described below (“annual financial information”):

- (i) annual financial statements of the Light System prepared in accordance with generally accepted accounting principles applicable to governmental units (except as otherwise noted therein), as such principles may be changed from time to time and as permitted by State law; which financial statements will not be audited, except that if and when audited financial statements are otherwise prepared and available to the City they will be provided;
- (ii) a statement of authorized, issued and outstanding bonded debt secured by Gross Revenues of the Light System;
- (iii) debt service coverage ratios;
- (iv) sources of Light System power and the cost thereof;
- (v) general customer statistics, such as number and type of customer and power consumed, and revenues by customer class; and
- (vi) average revenue per kWh of sales for each customer class.

Annual financial information described above will be provided to each NRMSIR and the SID, not later than the last day of the ninth month after the end of each fiscal year of the City, as such fiscal year may be changed as required or permitted by State law, commencing with the City’s fiscal year ending December 31, 2003. The annual financial information may be provided in a single or multiple documents, and may be incorporated by reference from other documents, including official statements of debt issues with respect to which the City is an obligated person as defined by the Rule, which documents have been filed with each NRMSIR and the SID. If the document incorporated is a “final official statement” (as defined by the Rule) with respect to which the City is an obligated person, it must be available from the Municipal Securities Rulemaking Board (“MSRB”).

The City also will provide or cause to be provided to each NRMSIR or the MSRB, and to the SID, timely notice of a failure by the City to provide the required annual financial information on or before the date specified above.

Material Events. The City further will provide or cause to be provided to each NRMSIR or the MSRB and the SID, timely notice of the occurrence of any of the following events with respect to the Bonds, if material:

- (i) principal and interest payment delinquencies;
- (ii) non-payment related defaults;
- (iii) unscheduled draws on debt service reserves reflecting financial difficulties;
- (iv) unscheduled draws on credit enhancements reflecting financial difficulties;
- (v) substitution of credit or liquidity providers, or their failure to perform;
- (vi) adverse tax opinions or events affecting the tax-exempt status of the Bonds;
- (vii) modifications to the rights of the holders of the Bonds;
- (viii) Bond calls (other than scheduled mandatory redemption of Term Bonds);
- (ix) defeasances;
- (x) release, substitution, or sale of property securing repayment of the Bonds; and
- (xi) rating changes.

For purposes of this section, “Continuing Disclosure Undertaking,” the term “holders of the Bonds” shall have the meaning intended for such term under the Rule.

Amendment of Undertaking. The Undertaking is subject to amendment without the consent of any holder of any Bond, or any broker, dealer, municipal securities dealer, participating underwriter, rating agency, NRMSIR, the SID or the MSRB, under the circumstances and in the manner permitted by the Rule.

The City will give notice to each NRMSIR or the MSRB, and the SID, of the substance (or provide a copy) of any amendment to the Undertaking and a brief statement of the reasons for the amendment. If the amendment changes the type of annual financial information to be provided, the annual financial information containing the amended information will include a narrative explanation of the effect of that change on the type of information to be provided.

Termination of Undertaking. The City’s obligations to provide annual financial information and notices of certain events will terminate upon the legal defeasance, prior redemption or payment in full of all of the then outstanding Bonds. In addition, the Undertaking, or any provision thereof, will be null and void if the City (i) obtains an opinion of nationally recognized bond counsel or other counsel familiar with the federal securities laws to the effect that those portions of the Rule which require the Undertaking, or any such provision, are invalid, have been repealed retroactively or otherwise do not apply to the Bonds; and (ii) notifies the SID and either the MSRB or each then existing NRMSIR of such termination.

Remedy for Failure to Comply with Undertaking. If the City fails to comply with the Undertaking, the City will proceed with due diligence to cause such noncompliance to be corrected as soon as practicable after the City learns of that failure.

No failure by the City or other obligated person to comply with the Undertaking will constitute a default in respect of the Bonds. The sole remedy of any holder of a Bond will be to take such actions as that holder deems necessary and appropriate to compel the City or other obligated person to comply with the Undertaking. The Undertaking will inure to the benefit of the City and any holder of the Bonds, and will not inure to the benefit of or create any rights in any other person.

Other Continuing Disclosure Undertakings of the City. The City has entered into undertakings to provide annual information and the notice of the occurrence of certain events with respect to all bonds issued by the City on and after July 3, 1995, subject to the Rule. The City is in compliance with all such undertakings.

OTHER BOND INFORMATION

Bond Insurance

Bond Insurance Policy. Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. ("Financial Security") will issue its Municipal Bond Insurance Policy for the Bonds (the "Policy"). The Policy guarantees the scheduled payment of principal of and interest on the Bonds when due as set forth in the form of the Policy included as Appendix F to this Official Statement.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut, or Florida insurance law.

Financial Security Assurance Inc. Financial Security is a New York domiciled insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. ("Holdings"). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At March 31, 2003, Financial Security's total policyholders' surplus and contingency reserves were approximately \$1,932,647,000 and its total unearned premium reserve was approximately \$1,077,095,000 in accordance with statutory accounting practices. At March 31, 2003, Financial Security's total shareholders' equity was approximately \$2,043,103,000 and its total net unearned premium reserve was approximately \$904,700,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Bonds or the advisability of investing in the Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the Department the information presented under this caption for inclusion in the Official Statement.

Ratings on the Bonds

The Bonds have been rated "Aaa" and "AAA" by Moody's Investors Service and Standard & Poor's Ratings Group, a Division of McGraw Hill, respectively, based upon the issuance of the Policy by Financial Security simultaneously with the delivery of the Bonds. The corresponding underlying ratings are "Aa3" and "A." The ratings reflect only the views of the rating agencies, and an explanation of the significance of the ratings may be obtained from each rating agency. No application was made to any other rating agency for the purpose of obtaining an additional rating on the Bonds. There is no assurance that the ratings will be retained for any given period of time or that the ratings will not be revised downward or withdrawn entirely by the rating agencies if, in their judgment, circumstances so warrant. Any such downward revision or withdrawal of the ratings will be likely to have an adverse effect on the market price of the Bonds.

Purchaser of the Bonds

The Bonds are being purchased by Lehman Brothers (the "Purchaser") at a price of \$264,250,394.40 and reoffered at a price of \$266,396,156.40, which reflects the yields set forth on the cover of this Official Statement. The Purchaser may offer and sell the Bonds to certain dealers (including dealers depositing Bonds

into investment trusts) and others at prices lower than the initial offering prices set forth on the inside of the cover hereof, and such initial offering prices may be changed from time to time by the purchaser. After the initial public offering, the public offering prices may be varied from time to time.

Official Statement

So far as any statements are made in this Official Statement involving matters of opinion or of estimates, whether or not so expressly stated, they are set forth as such and not as representations of fact, and no representation is made that any of the estimates will be realized. Information concerning the City, the Department and the Light System contained in this Official Statement has been furnished by the City. Neither this Official Statement nor any statement which may have been made orally or in writing is to be construed as a contract with the owners of any of the Bonds.

Neither the delivery of this Official Statement nor any sale of the Bonds will, under any circumstances, create any implication that there has been no change in the affairs of the Department since the date hereof. The City specifically disclaims any obligations to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of this Official Statement, except as otherwise expressly provided under “Legal and Tax Information—Continuing Disclosure Undertaking.”

The execution and delivery of this Official Statement have been duly authorized by the City.

THE CITY OF SEATTLE, WASHINGTON

/s/

Director of Finance

APPENDIX A
BOND ORDINANCE

(This page intentionally left blank.)

THE CITY OF SEATTLE, WASHINGTON

ORDINANCE 121198

AN ORDINANCE relating to the electric system of The City of Seattle; authorizing the issuance and sale of municipal light and power revenue bonds for the purposes of providing funds for certain additions and betterments to and extensions of the existing municipal light and power plant and system of the City, refunding all or a portion of certain of the City's outstanding municipal light and power revenue bonds, and paying the costs of issuing and selling the bonds authorized herein; providing for the terms, conditions, covenants and manner of sale of those bonds; and describing the lien of those bonds.

Passed June 23, 2003

TABLE OF CONTENTS

	<u>Page</u>
Section 1 . Definitions.....	2
Section 2 . Adoption of System or Plan; Authorization and Description of Bonds.....	14
Section 3 . Registration and Transfer or Exchange of Bonds	16
Section 4 . Mutilated, Lost, Stolen and Destroyed Bonds	20
Section 5 . Payment of Bond Principal and Interest	20
Section 6 . Redemption and Open Market Purchase of Bonds	21
(a) Optional Redemption.....	21
(b) Mandatory Redemption	21
(c) Partial Redemption.....	21
(d) Open Market Purchase.....	22
(e) Bonds to be Cancelled	22
Section 7 . Notice of Redemption	22
Section 8 . Failure to Redeem Bonds.....	23
Section 9 . Form and Execution of Bonds	23
Section 10 . Bond Registrar	24
Section 11 . Parity With Other Bonds.....	25
Section 12 . Execution of Refunding Plan(s).....	25
(a) Appointment of Refunding Trustee	25
(b) Acquisition and Substitution of Acquired Obligations	25
(c) Administration of Refunding Plan.....	26
(d) Authorization for Refunding Trust Agreement.....	26
Section 13 . Calls for Redemption of the Refunded Bonds	26
Section 14 . City Findings with Respect to Refunding.....	27
Section 15 . City Findings of Sufficiency of Revenues	27
Section 16 . Security for the Bonds	28
Section 17 . Bond Covenants	28
(a) Parity Bond Fund	28
(b) Reserve Fund	29
(c) Sale of Disposition of Light System	32
(d) Rates and Charges.....	33
(e) Maintenance and Operation of the Light System	33

1	(f) Books and Financial Statements	34
2	(g) Issuance of Future Parity Bonds	34
3	(h) Issuance of Refunding Parity Bonds	37
4	Section 18 . Preservation of Tax Exemption for Interest on Bonds	38
5	Section 19 . Advance Refunding or Defeasance of Bonds	39
6	Section 20 . Amendments	40
7	(a) Amendments Without Bond Owners’ Consent	40
8	(b) Amendments With Bond Owners’ Consent	41
9	(c) Effect of Amendment	42
10	(d) Notation on Bonds	42
11	Section 21 . Rate Stabilization Account	42
12	Section 22 . Sale of Bonds	42
13	Section 23 . Continuing Disclosure	43
14	Section 24 . General Authorization	43
15	Section 25 . Severability	44
16	Section 26 . Ratification of Prior Acts	44
17	Section 27 . Headings	44
18	Section 28 . Effective Date	45
19		
20		
21		
22		
23		
24		
25		
26		

ORDINANCE _____

AN ORDINANCE relating to the electric system of The City of Seattle; authorizing the issuance and sale of municipal light and power revenue bonds for the purposes of providing funds for certain additions and betterments to and extensions of the existing municipal light and power plant and system of the City, refunding all or a portion of certain of the City's outstanding municipal light and power revenue bonds, and paying the costs of issuing and selling the bonds authorized herein; providing for the terms, conditions, covenants and manner of sale of those bonds; and describing the lien of those bonds.

WHEREAS, The City of Seattle, Washington (the "City"), owns, operates and maintains an electric system (the "Light System"); and

WHEREAS, pursuant to Ordinance 116706 and Resolution 28751 (the "Refunded Bond Legislation") the City issued its Municipal Light and Power Revenue and Refunding Revenue Bonds, 1993 (the "1993 Bonds"), in the original principal amount of Four Hundred Fifty-Three Million Three Hundred Fifty-Five Thousand dollars (\$453,355,000), payable from and having a lien and charge on the Gross Revenues of the Light System prior and superior to all other charges whatsoever, except reasonable charges for maintenance and operation of the Light System; and

WHEREAS, there are presently outstanding One Hundred Thirty-nine Million One Hundred Ten Thousand dollars (\$139,110,000) par value of 1993 Bonds maturing or subject to mandatory redemption on May 1 and November 1 of each of the years 2004 through 2018, inclusive, and bearing interest at various rates ranging from 5.00% to 5.45%; and

WHEREAS, pursuant to the Refunded Bonds Legislation, the City reserved the right to redeem the 1993 Bonds maturing on or after May 1, 2004, as a whole or in part at any time on or after November 1, 2003, with the maturities to be redeemed to be selected by the City; and

WHEREAS, the City has need to acquire and construct certain additions and betterments to and extensions of the Light System described in the system or plan adopted by this ordinance (the "Plan of Additions"); and

WHEREAS, by the Refunded Bond Legislation, the City reserved the right to issue revenue bonds and other obligations having a charge and lien upon the Gross Revenue of the Light System on a parity with the charge and lien of the 1993 Bonds ("Parity Bonds") upon compliance with certain conditions described therein; and

WHEREAS, after due consideration, the City finds that it is necessary and in the best interest of the City and its ratepayers to issue municipal light and power revenue bonds on a parity of charge and lien with the 1993 Bonds and all other Parity Bonds then outstanding to pay part of the cost of the Plan of Additions, refund all or a portion of the 1993 Bonds and pay costs of issuing and selling those bonds; NOW, THEREFORE,

BE IT ORDAINED BY THE CITY OF SEATTLE AS FOLLOWS:

1 Section 1. Definitions. As used in this ordinance, the following words and phrases shall
2 have the meanings set forth below.

3 “Accreted Value” means with respect to any Capital Appreciation Bonds (a) as of any
4 Valuation Date, the amount set forth for such date in any Parity Bond Ordinance authorizing such
5 Capital Appreciation Bonds and (b) as of any date other than a Valuation Date, the sum of (i) the
6 Accreted Value on the preceding Valuation Date and (ii) the product of (A) a fraction, the numerator
7 of which is the number of days having elapsed from the preceding Valuation Date and the
8 denominator of which is the number of days from such preceding Valuation Date to the next
9 succeeding Valuation Date, calculated based on the assumption that Accreted Value accrues during
10 any semiannual period in equal daily amounts on the basis of a year of twelve 30-day months, times
11 (B) the difference between the Accreted Values for such Valuation Dates.

12 “Acquired Obligations” means those United States Treasury Certificates of Indebtedness,
13 Notes and Bonds--State and Local Government Series and other direct, noncallable obligations of
14 the United States of America purchased to accomplish the refunding of the Refunded Bonds as
15 authorized by this ordinance.

16 “Adjusted Net Revenue” has the meaning assigned to that term in Section 17(g)(iii).

17 “Annual Debt Service” for any calendar year means the sum of the amounts required in such
18 calendar year to pay:

19 (a) the interest due in such calendar year on all Parity Bonds outstanding, excluding
20 interest to be paid from the proceeds of the sale of Parity Bonds or other bonds; and

21 (b) the principal of all outstanding Serial Bonds due in such calendar year; and

22 (c) the Sinking Fund Requirement, if any, for such calendar year.

23 For purposes of this definition, the principal and interest portions of the Accreted Value of
24 Capital Appreciation Bonds becoming due at maturity or by virtue of a Sinking Fund Requirement
25 shall be included in the calculations of accrued and unpaid and accruing interest or principal in such
26

manner and during such period of time as is specified in any Parity Bond Ordinance authorizing such Capital Appreciation Bonds.

For purposes of calculating and determining compliance with the Reserve Fund Requirement and conditions for the issuance of Future Parity Bonds and/or entering into Parity Payment Agreements:

(i) Generally. Except as otherwise provided by subparagraph (ii) with respect to Variable Interest Rate Bonds and by subparagraph (iii) below with respect to Parity Bonds with respect to which a Payment Agreement is in force, interest on any issue of Parity Bonds shall be calculated based on the actual amount of accrued, accreted or otherwise accumulated interest that is payable in respect of that issue taken as a whole, at the rate or rates set forth in the applicable Parity Bond Ordinance;

(ii) Interest on Variable Interest Rate Bonds. The amount of interest deemed to be payable on any issue of Variable Interest Rate Bonds shall be calculated on the assumption that the interest rate on those bonds would be equal to the rate that is ninety percent (90%) of the average RBI during the four calendar quarters preceding the quarter in which the calculation is made;

(iii) Interest on Parity Bonds With Respect to Which a Payment Agreement is in Force. Debt service on Parity Bonds with respect to which a Payment Agreement is in force shall be based on the net economic effect on the City expected to be produced by the terms of the Parity Bonds and the terms of the Payment Agreement, including but not limited to the effects produced by the following: (A) Parity Bonds that would, but for a Payment Agreement, be treated as obligations bearing interest at a Variable Interest Rate instead shall be treated as obligations bearing interest at a fixed interest rate, and (B) Parity Bonds that would, but for a Payment Agreement, be treated as obligations bearing interest at a fixed interest rate instead shall be treated as obligations bearing interest at a Variable Interest Rate. Accordingly, the amount of interest deemed to be payable on any Parity Bonds with respect to which a Payment Agreement is in force shall be an amount equal to the amount of interest that would be payable at the rate or rates stated in those Parity Bonds plus

1 Payment Agreement Payments minus Payment Agreement Receipts. For the purposes of calculating
2 as nearly as practicable Payment Agreement Receipts and Payment Agreement Payments under a
3 Payment Agreement that includes a variable rate component determined by reference to a pricing
4 mechanism or index that is not the same as the pricing mechanism or index used to determine the
5 variable rate interest component on the Parity Bonds to which the Payment Agreement is related, it
6 shall be assumed that the fixed rate used in calculating Payment Agreement Payments will be equal
7 to 105% of the fixed rate specified by the Payment Agreement and that the pricing mechanism or
8 index specified by the Payment Agreement is the same as the pricing mechanism or index specified
9 by the Parity Bonds. Notwithstanding the other provisions of this subparagraph (iii), the City shall
10 not be required to (but may in its discretion) take into account in determining Annual Debt Service
11 the effects of any Payment Agreement that has a term of ten (10) years or less;

12 (iv) Parity Payment Agreements. No additional debt service shall be taken into
13 account with respect to a Parity Payment Agreement for any period during which Payment
14 Agreement Payments on that Parity Payment Agreement are taken into account in determining
15 Annual Debt Service on related Parity Bonds under subparagraph (iii) of this definition. However,
16 for any period during which Payment Agreement Payments are not taken into account in calculating
17 Annual Debt Service on any outstanding Parity Bonds because the Parity Payment Agreement is not
18 then related to any outstanding Parity Bonds, payments on that Parity Payment Agreement shall be
19 taken into account by assuming:

20 (A) City Obligated to Make Payments Based on Fixed Rate. If the City is
21 obligated to make Payment Agreement Payments based on a fixed rate and the Qualified
22 Counterparty is obligated to make payments based on a variable rate index, that payments by the
23 City will be based on the assumed fixed payor rate, and that payments by the Qualified Counterparty
24 will be based on a rate equal to the average rate determined by the variable rate index specified by
25 the Parity Payment Agreement during the four calendar quarters preceding the quarter in which the
26 calculation is made, and

1 (B) City Obligated to Make Payments Based on Variable Rate Index. If the
2 City is obligated to make Payment Agreement Payments based on a variable rate index and the
3 Qualified Counterparty is obligated to make payment based on a fixed rate, that payments by the
4 City will be based on a rate equal to the average rate determined by the variable rate index specified
5 by the Parity Payment Agreement during the four calendar quarters preceding the quarter in which
6 the calculation is made, and that the Qualified Counterparty will make payments based on the fixed
7 rate specified by the Parity Payment Agreement.

8 “Bond Counsel” means a lawyer or a firm of lawyers, selected by the City, of nationally
9 recognized standing in matters pertaining to bonds issued by states and their political subdivisions.

10 “Bond Register” means the books or records maintained by the Bond Registrar for the
11 purpose of registration of the Bonds.

12 “Bond Registrar” or “Registrar” means the fiscal agency of the State of Washington, or any
13 successor bond registrar selected by the City, whose duties include the registration and
14 authentication of the Bonds, maintenance of the Bond Register, effecting transfer of ownership of
15 the Bonds, and paying the principal of and premium, if any, and interest on the Bonds.

16 “Bond Resolution” means the resolution or resolutions fixing certain provisions of the Bonds
17 and their sale as authorized by Section 2 of this ordinance.

18 “Bonds” means the bonds authorized to be issued pursuant to, under the authority of and for
19 the purposes provided in this ordinance.

20 “1993 Bonds” means the Municipal Light and Power Revenue and Refunding Revenue
21 Bonds, 1993, of the City authorized by Ordinance 116706, as amended by Ordinance 117300, and
22 Resolution 28751.

23 “1994 Bonds” means the Municipal Light and Power Revenue Bonds, 1994, of the City
24 authorized by Ordinance 117374 and Resolution 29043.

1 “1995 Bonds” means, collectively, the Municipal Light and Power Revenue Bonds, 1995,
2 Series A and B, of the City authorized by Ordinance 117758 and Resolutions 29198 and 29218,
3 respectively.

4 “1996 Bonds” means the Municipal Light and Power Revenue Bonds, 1996, of the City
5 authorized by Ordinance 118282 and Resolution 29477.

6 “1997 Bonds” means the Municipal Light and Power Revenue Bonds, 1997, of the City
7 authorized by Ordinance 118745 and Resolution 29686.

8 “1998A Bonds” means the Municipal Light and Power Refunding Revenue Bonds, 1998,
9 Series A, of the City authorized by Ordinance 118744 and Resolution 29687.

10 “1998B Bonds” means the Municipal Light and Power Refunding Revenue Bonds, 1998,
11 Series B, of the City authorized by Ordinance 119141 and Resolution 29851.

12 “1999 Bonds” means the Municipal Light and Power Revenue Bonds, 1999, of the City
13 authorized by Ordinance 119638 and Resolution 30065.

14 “2000 Bonds” means the Municipal Light and Power Revenue Bonds, 2000, of the City
15 authorized by Ordinance 120131 and Resolution 30274.

16 “2001 Bonds” means the Municipal Light and Power Improvement and Refunding Revenue
17 Bonds, 2001, of the City authorized by Ordinance 120274 and Resolution 30298.

18 “2002 Bonds” means the Municipal Light and Power Refunding Revenue Bonds, 2002, of
19 the City authorized by Ordinance 120931 and Resolution 30549.

20 “Capital Appreciation Bonds” means any Parity Bonds as to which interest is payable only at
21 the maturity or prior redemption of such Parity Bonds. For the purpose of (a) receiving payment of
22 the redemption premium, if any, of a Capital Appreciation Bond that is redeemed prior to maturity,
23 or (b) computing the principal amount of Parity Bonds held by the owner of a Capital Appreciation
24 Bond in giving to the City or the paying agent for those bonds any notice, consent, request, or
25 demand pursuant to this ordinance or for any purpose whatsoever, the principal amount of a Capital
26 Appreciation Bond shall be deemed to be its Accreted Value.

1 “CIP” means the portion or portions relating to the Light System of the “2003-2008 Capital
2 Improvement Program” of the City as adopted by the City in Ordinance 120973, passed
3 November 18, 2002, as that CIP may be amended, updated, supplemented or replaced from time to
4 time.

5 “City” means The City of Seattle, Washington, a municipal corporation duly organized and
6 existing under the laws of the State of Washington.

7 “City Council” means the City Council of the City, as duly and regularly constituted from
8 time to time.

9 “Code” means the Internal Revenue Code of 1986, as amended, or any successor thereto, and
10 all applicable regulations thereunder.

11 “Conservation Plan” means the 1996 Energy Management Services Plan of the City with
12 respect to the Light System endorsed by the City in Resolution 29427, adopted September 16, 1996,
13 as that plan may be amended, updated, supplemented or replaced from time to time, to the extent that
14 funds are appropriated by the City therefor.

15 “Deferred Hydroelectric Project Relicensing Costs” means certain costs required by the
16 Federal Energy Regulatory Commission to be incurred as a condition of the renewal of licenses for
17 the Light System’s hydroelectric projects, which costs are treated in the same manner as capital
18 expenditures.

19 “DTC” means The Depository Trust Company, New York, New York, as initial Securities
20 Depository for the Bonds.

21 “Director of Finance” means the Director of Finance of the City, or any successor thereto.

22 “Future Parity Bonds” means any fixed or variable rate revenue bonds of the City (other than
23 the Bonds) issued hereafter having a charge or lien upon the Gross Revenues for payment of the
24 principal thereof and interest thereon equal in priority to the charge or lien upon the Gross Revenues
25 of the Light System for the payment of the principal of and interest on the Outstanding Parity Bonds
26

1 and the Bonds. Future Parity Bonds may include Parity Payment Agreements and any other
2 obligations issued in compliance with Section 17(g) or 17(h).

3 “Government Obligations” means direct obligations of, or obligations the principal of and
4 interest on which are unconditionally guaranteed by, the United States Government.

5 “Gross Revenues” means (a) all income, revenues, receipts and profits derived by the City
6 through the ownership and operation of the Light System; (b) the proceeds received by the City
7 directly or indirectly from the sale, lease or other disposition of any of the properties, rights or
8 facilities of the Light System; (c) Payment Agreement Receipts, to the extent that such receipts are
9 not offset by Payment Agreement Payments; and (d) the investment income earned on money held in
10 any fund or account of the City, including any bond redemption funds and the accounts therein, in
11 connection with the ownership and operation of the Light System. Gross Revenues do not include:
12 (A) insurance proceeds compensating the City for the loss of a capital asset; (B) income derived
13 from investments irrevocably pledged to the payment of any defeased bonds payable from Gross
14 Revenues; (C) investment income earned on money in any fund or account created or maintained
15 solely for the purpose of complying with the arbitrage rebate provisions of the Code; (D) any gifts,
16 grants, donations or other funds received by the City from any State or federal agency or other
17 person if such gifts, grants, donations or other funds are the subject of any limitation or reservation
18 imposed by the donor or grantor or imposed by law or administrative regulation to which the donor
19 or grantor is subject, limiting the application of such funds in a manner inconsistent with the
20 application of Gross Revenues hereunder; (E) the proceeds of any borrowing for capital
21 improvements (or the refinancing thereof); and (F) the proceeds of any liability or other insurance
22 (excluding business interruption insurance or other insurance of like nature insuring against the loss
23 of revenues).

24 “High Ross Agreement” means the agreement dated as of March 30, 1984, between the City
25 and Her Majesty the Queen in Right of the Province of British Columbia relating to the City’s High
26 Ross Dam.

1 “High Ross Capital Payments” means the deferred portion of the annual capital payments
2 required to be made by the City under Section 5 of the High Ross Agreement, representing the
3 annual cost that would have been incurred by the City for the construction of the High Ross Dam.

4 “Letter of Representations” means the Letter of Representations relating to the Bonds to be
5 delivered by the City to DTC.

6 “Light Fund” means the special fund of the City of that name heretofore created and
7 established by the City Council.

8 “Light System” means the municipal light and power plant and system now belonging to or
9 which may hereafter belong to the City.

10 “Mayor” means the Mayor of the City.

11 “Moody’s” means Moody’s Investors Service, Inc.

12 “Net Revenue” for any period has the meaning assigned to that term in Section 17(g).

13 “New Covenant Date” means the date on which no 1993 Bonds, 1994 Bonds, 1995 Bonds,
14 1996 Bonds, 1997 Bonds, 1998A Bonds, 1998B Bonds, 1999 Bonds or 2000 Bonds remain
15 outstanding under the respective ordinances authorizing the issuance of such bonds.

16 “Outstanding Parity Bonds” means, collectively, the outstanding 1993 Bonds, 1994 Bonds,
17 1995 Bonds, 1996 Bonds, 1997 Bonds, 1998A Bonds, 1998B Bonds, 1999 Bonds, 2000 Bonds,
18 2001 Bonds and 2002 Bonds.

19 “Parity Bond Fund” means the Seattle Municipal Light Revenue Parity Bond Fund
20 established pursuant to Ordinance 92938 and now treated as a separate account within the Light Fund.

21 “Parity Bond Ordinance” means any ordinance or resolution passed or adopted by the City
22 Council providing for the issuance of Parity Bonds, and any other ordinance or resolution amending
23 or supplementing the provisions of any Parity Bond Ordinance as originally passed or adopted or as
24 theretofore amended or supplemented.

25 “Parity Bonds” means the Outstanding Parity Bonds, the Bonds and any Future Parity Bonds.
26

1 “Parity Payment Agreement” means a Payment Agreement under which the City’s
2 obligations are expressly stated to constitute a charge and lien on the Net Revenue of the Light
3 System equal in rank with the charge and lien upon such Net Revenue required to be paid into the Parity
4 Bond Fund to pay and secure the payment of the principal of and interest on Parity Bonds.

5 “Payment Agreement” means a written contract entered into, for the purpose of managing or
6 reducing the City’s exposure to fluctuations or levels of interest rates or for other interest rate,
7 investment, asset or liability management purposes, by the City and a Qualified Counterparty on
8 either a current or forward basis as authorized by any applicable laws of the State in connection with,
9 or incidental to, the issuance, incurring or carrying of particular bonds, notes, bond anticipation
10 notes, commercial paper or other obligations for borrowed money, or lease, installment purchase or
11 other similar financing agreements or certificates of participation therein, that provides for an
12 exchange of payments based on interest rates, ceilings or floors on such payments, options on such
13 payments, or any combination thereof or any similar device.

14 “Payment Agreement Payments” means the amounts, periodically required to be paid by the
15 City to the Qualified Counterparty pursuant to a Payment Agreement.

16 “Payment Agreement Receipts” means the amounts periodically required to be paid by the
17 Qualified Counterparty to the City pursuant to a Payment Agreement.

18 “Permitted Investments” means any investments or investment agreements permitted for the
19 investment of City funds under the laws of the State of Washington as amended from time to time.

20 “Plan of Additions” means, collectively, the CIP and the Conservation Plan, as they may be
21 modified hereafter by ordinance as described herein, the High Ross Capital Payments and the
22 Deferred Hydroelectric Project Relicensing Costs.

23 “Professional Utility Consultant” means the independent person(s) or firm(s) selected by the
24 City having a favorable reputation for skill and experience with electric systems of comparable size
25 and character to the Light System in such areas as are relevant to the purposes for which they were
26 retained.

1 “Qualified Counterparty” means a party (other than the City or a person related to the City)
2 who is the other party to a Payment Agreement and who is qualified to act as the other party to a
3 Payment Agreement under any applicable laws of the State.

4 “Qualified Insurance” means any municipal bond insurance policy or surety bond issued by
5 any insurance company licensed to conduct an insurance business in any state of the United States
6 (or by a service corporation acting on behalf of one or more such insurance companies) which
7 insurance company or companies, as of the time of issuance of such policy or surety bond, are rated in
8 one of the two highest rating categories by Moody’s and S&P or their comparably recognized business
9 successors.

10 “Qualified Letter of Credit” means any letter of credit issued by a financial institution for the
11 account of the City on behalf of the owners of Parity Bonds, which institution maintains an office,
12 agency or branch in the United States and as of the time of issuance of such letter of credit is rated in
13 one of the two highest rating categories by Moody’s and S&P or their comparably recognized
14 business successors.

15 “Rate Stabilization Account” means the fund of that name created in the Light Fund for the
16 purposes described in this ordinance.

17 “RBI” means The Bond Buyer Revenue Bond Index or comparable index, or, if no
18 comparable index can be obtained, eighty percent (80%) of the interest rate for actively traded thirty
19 (30) year United States Treasury obligations.

20 “Refunded Bonds” means all or that portion of the 1993 Bonds included in a Refunding Plan.

21 “Refunded Bond Ordinance” means one or more of the ordinances and resolutions pursuant
22 to which the Refunded Bonds were issued.

23 “Refunding Parity Bonds” means Parity Bonds issued for the purpose of refunding bonds of
24 any prior series of Parity Bonds.

25 “Refunding Plan” means, for any series of Bonds:
26

1 (a) the placement of sufficient proceeds of the Bonds which, with other money of the
2 City, if necessary, will acquire the Acquired Obligations, if any, to be deposited, with cash, if
3 necessary, with the Refunding Trustee;

4 (b) the payment of the principal of and interest on the Refunded Bonds when due up to
5 and including the date set forth in the Bond Resolution, and the call, payment and redemption on that
6 date of all or a portion of the then-outstanding Refunded Bonds, at the price set forth in the Bond
7 Resolution; and

8 (c) the payment of the costs of issuing the Bonds and the costs of carrying out the
9 foregoing elements of the Refunding Plan.

10 “Refunding Trust Agreement” means the Refunding Trust Agreement between the City and a
11 Refunding Trustee relating to a particular series of Bonds.

12 “Refunding Trustee” means the trustee or escrow agent, or any successor trustee or escrow
13 agent, with respect to a particular series of Bonds, designated by the Director of Finance.

14 “Reserve Fund” means the Municipal Light and Power Bond Reserve Fund established
15 pursuant to Ordinance 71917, as amended, and now treated as a separate account within the Light
16 Fund.

17 “Reserve Fund Requirement” means, at any time, the lesser of (a) the maximum Annual Debt
18 Service on all Parity Bonds then outstanding; and (b) the maximum amount permitted by the Code as
19 a “reasonably required reserve or replacement fund.” *Notwithstanding the foregoing, on the New*
20 *Covenant Date, “Reserve Fund Requirement” shall mean, for any issue of Future Parity Bonds, the*
21 *Reserve Fund Requirement specified for that issue, and the Reserve Fund Requirement for all series of*
22 *Future Parity Bonds shall be the sum of the Reserve Fund Requirement for all such Future Parity*
23 *Bonds.*

24 “S&P” means Standard & Poor’s Ratings Services, a Division of The McGraw-Hill
25 Companies, Inc.

1 “Securities Depository” means any one of the following registered securities depositories
2 which has been designated by the City: (i) DTC; (ii) Midwest Securities Trust Company, Chicago,
3 Illinois, (iii) Philadelphia Depository Trust Company, Philadelphia, Pennsylvania; or (iv) such other
4 securities depositories as the City may designate in a certificate of the City delivered to the Bond
5 Registrar.

6 “Serial Bonds” means Parity Bonds maturing in specified years, for which no Sinking Fund
7 Requirements are mandated.

8 “Sinking Fund Account” means any account created in the Parity Bond Fund to amortize the
9 principal or make mandatory redemptions of Term Bonds.

10 “Sinking Fund Requirement” means, for any calendar year, the principal amount and
11 premium, if any, of Term Bonds required to be purchased, redeemed, paid at maturity or paid into
12 any Sinking Fund Account for such calendar year as established by the Parity Bond Ordinance
13 authorizing the issuance of such Term Bonds.

14 “State” means the State of Washington.

15 “Subordinate Lien Bonds” means, collectively, the City’s outstanding Municipal Light and
16 Power Adjustable Rate Revenue Bonds, 1990, Municipal Light and Power Adjustable Rate Revenue
17 Bonds, 1991, Series A and B, Municipal Light and Power Adjustable Rate Revenue Bonds, 1993,
18 and Municipal Light and Power Adjustable Rate Revenue Bonds, 1996, and any bonds issued
19 hereafter, having a charge or lien upon the Gross Revenues of the Light System on a parity with
20 those bonds.

21 “Term Bonds” means any Parity Bonds identified as such in the Parity Bond Ordinance
22 authorizing the issuance thereof, which Parity Bond Ordinance requires that all or a portion of such
23 bonds be purchased, redeemed or paid prior to maturity in a schedule established thereby.

24 “Valuation Date” means, with respect to any Capital Appreciation Bonds, the date or dates
25 set forth in any Parity Bond Ordinance authorizing such Parity Bonds on which specific Accreted
26 Values are assigned to the Capital Appreciation Bonds.

1 “Variable Interest Rate” means any variable interest rate or rates to be borne by any Parity
2 Bonds. The method of computing such a variable interest rate shall be as specified in the Parity
3 Bond Ordinance authorizing or specifying the terms of such Parity Bonds, which Parity Bond
4 Ordinance also shall specify either (i) the particular period or periods of time or manner of
5 determining such period or periods of time for which each value of such variable interest rate shall
6 remain in effect or (ii) the time or times upon which any change in such variable interest rate shall
7 become effective.

8 “Variable Interest Rate Bonds” means, for any period of time, any Parity Bonds that bear a
9 Variable Interest Rate during that period, except that Parity Bonds shall not be treated as Variable
10 Interest Rate Bonds if the net economic effect of interest rates on particular Parity Bonds of an issue
11 and interest rates on other Parity Bonds of the same issue, as set forth in the applicable Parity Bond
12 Ordinance, or the net economic effect of a Payment Agreement with respect to particular Parity
13 Bonds, in either case is to produce obligations that bear interest at a fixed interest rate; and Parity
14 Bonds with respect to which a Payment Agreement is in force shall be treated as Variable Interest
15 Rate Bonds if the net economic effect of the Payment Agreement is to produce obligations that bear
16 interest at a Variable Interest Rate.

17 Section 2. Adoption of System or Plan; Authorization and Description of Bonds. The
18 Plan of Additions constitutes a system or plan of additions to and betterments and extensions of the
19 Light System (each element thereof an “Addition”). To the extent not previously specified, adopted
20 and ordered by the City by ordinance, the City specifies, adopts and orders to be carried out the Plan
21 of Additions, and declares the estimated cost of that system or plan to be Nine Hundred Fifty-Two
22 Million Five Hundred Seventy-Nine Thousand Dollars (\$952,579,000), of which One Hundred Forty
23 Million Dollars (\$140,000,000) is expected to be financed from proceeds of the Bonds.

24 The Plan of Additions shall include any amendments, updates, supplements or replacements
25 to the CIP or the Conservation Plan determined by ordinance to constitute a system or plan of
26 additions to and betterments and extensions of the Light System, all of which automatically shall

1 constitute amendments to the Plan of Additions. The Plan of Additions also may be modified,
2 without amending the CIP or the Conservation Plan, to include other elements if the City determines
3 by ordinance that those other elements constitute a system or plan of additions to or betterments or
4 extensions of the Light System. The Plan of Additions includes the purchase and installation of all
5 materials, supplies, appliances, equipment (including but not limited to data processing hardware
6 and software and conservation equipment) and facilities, the acquisition of all permits, licenses,
7 franchises, property and property rights, other capital assets and all engineering, consulting and other
8 professional services and studies (whether performed by the City or by other public or private
9 entities) necessary or convenient to carry out the Plan of Additions.

10 For the purpose of providing all or part of the funds with which to (1) pay part of the cost of
11 carrying out the Plan of Additions; (2) refund all or a portion of the Refunded Bonds; and (4) pay the
12 costs of issuing and selling the Bonds, the City shall issue and sell the Bonds in the aggregate
13 principal amount of not to exceed Two Hundred Eighty Million Dollars (\$280,000,000). The Bonds
14 may be issued in one or more series, except that the final series shall be issued on or before
15 December 31, 2004; may be combined with other Parity Bonds authorized separately; shall be called
16 “The City of Seattle, Washington, Municipal Light and Power Improvement and Refunding Revenue
17 Bonds, 2003” (unless changed by resolution); may have such different or further designation or
18 designations as determined by the Director of Finance or as the City Council may specify in a
19 resolution or resolutions fixing the terms of and matters relating to the Bonds (collectively, the
20 “Bond Resolution”); shall be dated and shall mature on such date or dates specified in the Bond
21 Resolution, except that the final maturity date of the Bonds shall not extend beyond December 31,
22 2034; shall be issued in fully registered form; shall be numbered separately in the manner and with
23 any additional designation as the Bond Registrar for the Bonds deems necessary for purposes of
24 identification; shall bear interest at the rate or rates (computed on the basis of a 360-day year of
25 twelve 30-day months) specified in the Bond Resolution, except that the net interest cost shall not
26 exceed a weighted average rate of 7.5% per annum, payable at the times specified in the Bond

1 Resolution; and shall have such denominations, mature on such dates and be subject to optional or
2 mandatory redemption, open market purchase or defeasance on the terms and at the times specified
3 in the Bond Resolution. The Director of Finance may designate Term Bonds with mandatory
4 redemption amounts, all to be provided by the Bond Resolution. The Director of Finance also may
5 specify in the Bond closing documents the respective amounts of each maturity of the Bonds
6 allocated to paying the costs of carrying out the Plan of Additions and the Refunding Plan.

7 The City Council may adopt the Bond Resolution and may provide therein for the matters
8 described in this ordinance, including the manner of sale of the Bonds, which may include a forward
9 or delayed delivery, and such other matters that the City Council deems necessary and appropriate to
10 carry out the purposes of this ordinance. Once adopted, the Bond Resolution shall be deemed a part
11 of this ordinance as if set forth herein.

12 The Bond Resolution may provide for Qualified Insurance or a Qualified Letter of Credit,
13 and conditions or covenants relating thereto, including additional terms, conditions and covenants
14 relating to the Bonds that are required by the bond insurer or letter of credit provider and are
15 consistent with the provisions of this ordinance, including but not limited to restrictions on
16 investments and requirements of notice to and consent of the bond insurer or letter of credit provider.

17 The Bond Resolution may approve and authorize the execution and delivery on behalf of the
18 City of any contracts consistent with the provisions of this ordinance for which the City's approval is
19 necessary or to which the City is a party and that are related or incidental to the initial issuance and
20 sale of the Bonds, the initial establishment of the interest rate or rates on the Bonds and any
21 redemption of the Bonds, including but not limited to Payment Agreements and similar contracts for
22 such purposes.

23 Section 3. Registration and Transfer or Exchange of Bonds. The Bonds shall be issued
24 only in registered form as to both principal and interest and recorded on the Bond Register. The
25 Bond Register shall contain the name and mailing address of the registered owner of each Bond and
26 the principal amount and number of each of the Bonds held by each registered owner.

1 Bonds surrendered to the Bond Registrar may be exchanged for Bonds in any authorized
2 denomination of an equal aggregate principal amount and of the same series, interest rate and
3 maturity. Bonds may be transferred only if endorsed in the manner provided thereon and
4 surrendered to the Bond Registrar. Any exchange or transfer shall be without cost to the registered
5 owner or transferee. The Bond Registrar shall not be obligated to exchange or transfer any Bond
6 during the period between any record date and the next succeeding principal or interest payment or
7 redemption date.

8 The City appoints DTC as initial Securities Depository for the Bonds. For so long as DTC is
9 the Securities Depository for the Bonds, DTC shall be deemed to be the registered owner of the
10 Bonds for all purposes hereunder, and all references in this ordinance or the Bond Resolution to the
11 registered owners of the Bonds shall mean DTC or its nominee and shall not mean the owners of any
12 beneficial interests in the Bonds. Payments of principal of and interest on all outstanding Bonds
13 registered in the name of the nominee of DTC, or its registered assign, shall be made as provided in
14 the Letter of Representations.

15 Bonds executed and delivered in fully immobilized form shall be executed and delivered in
16 the form of one fully-registered immobilized certificate for each series and maturity of the Bonds
17 representing the aggregate principal amount of the Bonds of that series and maturity, which Bonds
18 shall (except as provided below for the discontinuation or substitution of Securities Depository) be
19 registered in the name of the Securities Depository or its nominee. For so long as DTC serves as
20 Securities Depository for the Bonds, the Bonds shall be registered in the name of Cede & Co., as
21 nominee of DTC; however, if DTC shall request that the Bonds be registered in the name of a
22 different nominee, the Bond Registrar shall exchange all or any portion of the Bonds for an equal
23 aggregate principal amount of Bonds registered in the name of such other nominee or nominees of
24 DTC. No person other than DTC or its nominee shall be entitled to receive from the City or the
25 Bond Registrar any Bond or any other evidence of ownership of the Bonds, or any right to receive
26 any payment in respect thereof, unless DTC or its nominee shall transfer record ownership of all or

1 any portion of the Bonds on the Bond Register, in connection with discontinuing the book-entry
2 system as provided below or otherwise.

3 So long as the Bonds are registered in the name of DTC or any nominee thereof, all payments
4 of the principal of, premium, if any, or interest on the Bonds shall be made to DTC or its nominee in
5 immediately available funds on the dates provided for such payments under this ordinance and the
6 Bond Resolution and at such times and in the manner provided in the Letter of Representations.
7 Each such payment to DTC or its nominee shall be valid and effective to fully discharge all liability
8 of the City or the Bond Registrar with respect to the principal of, premium, if any, or interest on the
9 Bonds to the extent of the sum or sums so paid. In the event of the redemption of less than all of the
10 Bonds of any series and maturity, the Bond Registrar shall not require surrender by DTC or its
11 nominee of the Bonds so redeemed, and DTC or its nominee may retain such Bonds and make an
12 appropriate notation thereon as to the amount of such partial redemption. DTC shall deliver to the
13 Bond Registrar, upon request, a written confirmation of such partial redemption. The records
14 maintained by the Bond Registrar shall be conclusive as to the amount of the Bonds of such series
15 and maturity that have been redeemed.

16 All transfers of beneficial ownership interests in Bonds registered in the name of DTC or its
17 nominee shall be effected by the procedures of DTC's participants and/or indirect participants for
18 recording and transferring the ownership of beneficial interests in bonds.

19 The City and the Bond Registrar may treat DTC, or any nominee thereof, as the sole and
20 exclusive registered owner of the Bonds registered in such name for the purposes of payment of the
21 principal of, premium, if any, or interest on those Bonds, selecting Bonds or portions thereof to be
22 redeemed, giving any notice permitted or required to be given to registered owners of Bonds under
23 this ordinance or the Bond Resolution, registering the transfer of Bonds, obtaining any consent or other
24 action to be taken by registered owners of Bonds and for all other purposes whatsoever; and the City
25 and the Bond Registrar shall not be affected by any notice to the contrary. The City and the Bond
26 Registrar shall not have any responsibility or obligation to any direct or indirect DTC participant, any

1 person claiming a beneficial ownership interest in the Bonds under or through DTC or any such direct
2 or indirect participant, or any other person which is not shown on the Bond Register as being a
3 registered owner of Bonds, with respect to: (1) the Bonds; (2) any records maintained by DTC or any
4 such direct or indirect participant; (3) the payment by DTC or any such direct or indirect participant of
5 any principal of, premium, if any, or interest on the Bonds; (4) any notice which is permitted or required
6 to be given to registered owners of Bonds under this ordinance or the Bond Resolution; (5) the selection
7 by DTC or any direct or indirect participant of any person to receive payment in the event of a partial
8 redemption of the Bonds; or (6) any consent given or other action taken by DTC as registered owner of
9 the Bonds.

10 So long as the Bonds are registered in the name of DTC or any nominee thereof, all notices
11 required or permitted to be given to the registered owners of such Bonds under this ordinance or the
12 Bond Resolution shall be given to DTC as provided in the Letter of Representations, in form and
13 content satisfactory to DTC, the City and the Bond Registrar.

14 In connection with any notice or other communication to be provided to registered owners
15 pursuant to this ordinance or the Bond Resolution by the City or the Bond Registrar with respect to
16 any consent or other action to be taken by registered owners of the Bonds, DTC shall consider the
17 date of receipt of notice requesting such consent or other action as the record date for such consent
18 or other action; however, the City or the Bond Registrar may establish a special record date for such
19 consent or other action and shall give DTC notice of such special record date not less than fifteen
20 (15) calendar days in advance of such special record date to the extent possible.

21 Any successor Bond Registrar, in its written acceptance of its duties under this ordinance and
22 the Bond Resolution, shall agree to take any actions necessary from time to time to comply with the
23 requirements of the Letter of Representations.

24 The book-entry system for registration of the ownership of the Bonds in fully immobilized
25 form may be discontinued at any time if: (1) after notice to the City and the Bond Registrar, DTC
26 determines to resign as Securities Depository for the Bonds; or (2) after notice to DTC and the Bond

1 Registrar, the City determines that a continuation of the system of book-entry transfers through DTC (or
2 through a successor Securities Depository) is not in the best interests of the City. In each of such events
3 (unless, in the case described in clause (1) above, the City appoints a successor Securities Depository),
4 the Bonds shall be delivered in registered certificate form to such persons, and in such maturities and
5 principal amounts, as may be designated by DTC, but without any liability on the part of the City or the
6 Bond Registrar for the accuracy of such designation. Whenever DTC requests the City and the Bond
7 Registrar to do so, or whenever the City requests DTC and the Bond Registrar to do so after the
8 determination by the City to replace DTC with a successor Securities Depository, the City and the Bond
9 Registrar shall cooperate with DTC in taking appropriate action after reasonable notice to arrange for
10 another Securities Depository to maintain custody of certificates evidencing the Bonds.

11 Section 4. Mutilated, Lost, Stolen and Destroyed Bonds. In case any Bonds issued
12 hereunder shall become mutilated or be destroyed, stolen or lost, the City may, if not then prohibited
13 or otherwise required by law, cause to be executed and delivered a new Bond of like amount, series,
14 interest rate, maturity date and tenor in exchange and substitution for and upon cancellation of such
15 mutilated Bonds, or in lieu of and in substitution for such destroyed, stolen or lost Bonds, upon
16 payment by the registered owner thereof of the reasonable expenses and charges of the City and the
17 Bond Registrar in connection therewith, and in the case of a Bond destroyed, stolen or lost, the filing
18 with the Bond Registrar of evidence satisfactory to the City that such Bond was destroyed, stolen or
19 lost, and of the ownership thereof, and furnishing the City and the Bond Registrar with indemnity
20 satisfactory to each of them. If the mutilated, destroyed, stolen or lost Bond already has matured or
21 been called for redemption in accordance with its terms it shall not be necessary to issue a new Bond
22 prior to payment.

23 Section 5. Payment of Bond Principal and Interest. Principal of, premium, if any, on and
24 interest on the Bonds shall be payable in lawful money of the United States of America. Interest on
25 the Bonds shall be paid by checks or drafts mailed by the Bond Registrar on the interest payment
26 date to the registered owners at the addresses appearing on the Bond Register on the fifteenth day of

1 the month preceding the interest payment date (or other record date established in the Bond
2 Resolution, the “Record Date”) or, at the request of the registered owner of One Million dollars
3 (\$1,000,000) or more in aggregate principal amount of Bonds, by wire transfer to an account in the
4 United States designated in writing by such registered owner prior to the Record Date. Principal of
5 and premium, if any, on the Bonds shall be payable upon presentation and surrender of the Bonds by
6 the registered owners at either of the principal corporate trust office or offices of the Bond Registrar
7 at the option of the owners. Notwithstanding the foregoing, payment of any Bonds registered in the
8 name of DTC or its nominee, shall be made in accordance with the Letter of Representations.

9 The Bonds shall be payable solely out of the Parity Bond Fund and shall not be general
10 obligations of the City.

11 Section 6. Redemption and Open Market Purchase of Bonds.

12 (a) Optional Redemption. All or some of the Bonds may be subject to redemption at the
13 option of the City at the times and on the terms set forth in the Bond Resolution.

14 (b) Mandatory Redemption. The City shall redeem any Term Bonds, if not redeemed under
15 the optional redemption provisions set forth in the Bond Resolution or purchased in the open market
16 under the provisions set forth below, by lot (or in such other manner as the Bond Registrar shall
17 determine) at par plus accrued interest on the dates and in the years and principal amounts as set
18 forth in the Bond Resolution.

19 If the City redeems Term Bonds under the optional redemption provisions set forth in the
20 Bond Resolution or purchases Term Bonds in the open market as set forth below, the Term Bonds so
21 redeemed or purchased (irrespective of their redemption or purchase price) shall be credited at the
22 par amount thereof against the remaining mandatory redemption requirements in a manner to be
23 determined by the Director of Finance or, if no such determination is made, on a pro-rata basis.

24 (c) Partial Redemption. Whenever less than all of the Bonds of a single maturity are to be
25 redeemed, the Bond Registrar shall select the Bonds or portions thereof to be redeemed from the
26 Bonds of that maturity by lot, or in such other manner as the Bond Registrar shall determine, except

1 that, so long as the Bonds are registered in the name of DTC or its nominee, DTC shall select the
2 Bonds or portions thereof to be redeemed in accordance with the Letter of Representations. In no
3 event shall any Bond be outstanding in a principal amount that is not an authorized denomination.

4 Portions of the principal amount of any Bond, in integral multiples of Five Thousand dollars
5 (\$5,000), may be redeemed, unless otherwise provided in the Bond Resolution. If less than all of the
6 principal amount of any Bond is redeemed, upon surrender of that Bond at either of the principal
7 offices of the Bond Registrar, there shall be issued to the registered owner, without charge therefor, a
8 new Bond (or Bonds, at the option of the registered owner) of the same series, maturity and interest
9 rate in any of the denominations authorized by the Bond Resolution in the aggregate total principal
10 amount remaining unredeemed.

11 (d) Open Market Purchase. The City reserves the right and option to purchase any or all of
12 the Bonds in the open market at any time at any price acceptable to the City plus accrued interest to
13 the date of purchase.

14 (e) Bonds to be Cancelled. All Bonds purchased or redeemed under this Section 6 shall be
15 cancelled.

16 Section 7. Notice of Redemption. The City shall cause notice of any intended
17 redemption of Bonds to be given not less than thirty (30) nor more than sixty (60) days prior to the
18 date fixed for redemption by first-class mail, postage prepaid, to the registered owner of any Bond to
19 be redeemed at the address appearing on the Bond Register at the time the Bond Registrar prepares
20 the notice, and the requirements of this sentence shall be deemed to have been fulfilled when notice
21 has been mailed as so provided, whether or not it is actually received by the registered owner of any
22 Bond. Interest on Bonds called for redemption shall cease to accrue on the date fixed for redemption
23 unless the Bond or Bonds called are not redeemed when presented pursuant to the call. In addition,
24 the redemption notice shall be mailed by the Bond Registrar within the same period, postage
25 prepaid, to Moody's and S&P at their offices in New York, New York, or their successors, to any
26 bond insurer for the Bonds, and to such other persons and with such additional information as the

1 Director of Finance shall determine or as specified in the Bond Resolution, but these additional
2 mailings shall not be a condition precedent to the redemption of Bonds.

3 Section 8. Failure to Redeem Bonds. If any Bond is not redeemed when properly
4 presented at its maturity or call date, the City shall be obligated to pay interest on that Bond at the
5 same rate provided in the Bond from and after its maturity or call date until that Bond, principal,
6 premium, if any, and interest, is paid in full or until sufficient money for its payment in full is on
7 deposit in the Parity Bond Fund and the Bond has been called for payment by giving notice of that
8 call to the registered owner of each of those unpaid Bonds.

9 Section 9. Form and Execution of Bonds. The Bonds shall be typed, photocopied,
10 printed or lithographed on good bond paper in a form consistent with the provisions of this
11 ordinance, the Bond Resolution and State law; shall be signed by the Mayor and Director of Finance,
12 either or both of whose signatures may be manual or in facsimile; and the seal of the City or a
13 facsimile reproduction thereof shall be impressed or printed thereon.

14 Only Bonds bearing a Certificate of Authentication in substantially the following form,
15 manually signed by the Bond Registrar, shall be valid or obligatory for any purpose or entitled to the
16 benefits of this ordinance:

17 CERTIFICATE OF AUTHENTICATION

18 This Bond is one of the fully registered The City of Seattle, Washington,
19 Municipal Light and Power Improvement and Refunding Revenue Bonds, 2003,
described in the Bond Ordinance.

20 Bond Registrar

21 By _____
22 Authorized Signer

23
24 The authorized signing of a Certificate of Authentication shall be conclusive evidence that the Bond
25 so authenticated has been duly executed, authenticated and delivered and is entitled to the benefits of
26 this ordinance.

1 If any officer whose facsimile signature appears on the Bonds ceases to be an officer of the
2 City authorized to sign bonds before the Bonds bearing his or her facsimile signature are
3 authenticated or delivered by the Bond Registrar or issued by the City, those Bonds nevertheless
4 may be authenticated, delivered and issued and, when authenticated, issued and delivered, shall be as
5 binding on the City as though that person had continued to be an officer of the City authorized to
6 sign bonds. Any Bond also may be signed on behalf of the City by any person who, on the actual
7 date of signing of the Bond, is an officer of the City authorized to sign bonds, although he or she did
8 not hold the required office on the date of issuance of the Bonds.

9 Section 10. Bond Registrar. The Bond Registrar shall keep, or cause to be kept, at its
10 principal corporate trust office, sufficient books for the registration and transfer of the Bonds which
11 shall be open to inspection by the City at all times. The Bond Registrar is authorized, on behalf of
12 the City, to authenticate and deliver Bonds transferred or exchanged in accordance with the
13 provisions of the Bonds and this ordinance, to serve as the City's paying agent for the Bonds and to
14 carry out all of the Bond Registrar's powers and duties under this ordinance and SMC Chapter 5.10
15 establishing a system of registration for the City's bonds and obligations, as that chapter now exists
16 or may hereafter be amended. The City reserves the right in its discretion to appoint special paying
17 agents, registrars or trustees in connection with the payment of some or all of the principal of or
18 interest on the Bonds. If a new Bond Registrar is appointed by the City, notice of the name and
19 address of the new Bond Registrar shall be mailed to the registered owners of the Bonds. The notice
20 may be mailed together with the next interest payment due on the Bonds, but, to the extent
21 practicable, shall be mailed not less than fifteen (15) days prior to a maturity date of the principal of
22 any Bond.

23 The Bond Registrar shall be responsible for its representations contained in the Bond
24 Registrar's Certificate of Authentication on the Bonds. The Bond Registrar may become the
25 registered owner of Bonds with the same rights it would have if it were not the Bond Registrar and,
26 to the extent permitted by law, may act as depository for and permit any of its officers or directors to

1 act as members of, or in any other capacity with respect to, any committee formed to protect the
2 rights of the registered owners of the Bonds.

3 Section 11. Parity With Other Bonds. The Bonds authorized herein shall be on a parity
4 with the Outstanding Parity Bonds and all bonds hereafter issued on a parity therewith, without
5 regard to date of issuance or authorization and without preference or priority of right or lien with
6 respect to participation of special funds in amounts from gross revenues for payment thereof.
7 Nothing contained herein shall prevent the City from issuing revenue bonds or other obligations
8 which are a charge or lien upon the Gross Revenues of the Light System subordinate to the payments
9 required to be made therefrom into the Parity Bond Fund and the accounts therein.

10 Section 12. Execution of Refunding Plan(s).

11 (a) Appointment of Refunding Trustee. The Refunding Trustee, if any, for each series of
12 Refunded Bonds shall be designated by the Director of Finance and confirmed by the Bond
13 Resolution.

14 (b) Acquisition and Substitution of Acquired Obligations. If the Bonds of a series include
15 Bonds to carry out all or a portion of the Refunding Plan, sufficient proceeds of the sale of the Bonds
16 shall be deposited immediately upon the receipt thereof with the Bond Registrar for the Refunded
17 Bonds or with the Refunding Trustee, as specified in the Bond Resolution, and used to discharge the
18 obligations of the City relating to the Refunded Bonds to be refunded therewith under the Refunded
19 Bond Ordinance by providing for the payment of the amounts required to be paid by the Refunding
20 Plan. The Refunding Plan shall be carried out, and proceeds of the Bonds allocable to the refunding
21 purposes shall be applied, in accordance with this ordinance, the Refunded Bond Ordinance, the
22 Bond Resolution and the laws of the State. To the extent practicable, such obligations shall be
23 discharged fully by the Refunding Trustee's simultaneous purchase of the Acquired Obligations,
24 bearing such interest and maturing as to principal and interest in such amounts and at such times so
25 as to provide, together with a beginning cash balance, if necessary, for the payment of the amount
26 required to be paid by the Refunding Plan. The Acquired Obligations shall be listed and more

1 particularly described in a schedule attached to the Refunding Trust Agreement, and shall be subject
2 to substitution as set forth therein. Any surplus money resulting from the sale, transfer, other
3 disposition or redemption of the Acquired Obligations and the substitutions therefor shall be released
4 from the trust estate and transferred to the Light Fund to be used for any lawful purpose.

5 (c) Administration of Refunding Plan. The Refunding Trustee is authorized and directed to
6 purchase the Acquired Obligations (or substitute obligations) and to make the payments required to
7 be made by the Refunding Plan from the Acquired Obligations (or substitute obligations) and money
8 deposited with the Refunding Trustee pursuant to this ordinance. All Acquired Obligations (or
9 substitute obligations) and the money deposited with the Refunding Trustee and any income
10 therefrom shall be held irrevocably, invested and applied in accordance with the provisions of the
11 Refunded Bond Ordinance, this ordinance, the Bond Resolution, chapter 39.53 RCW and other
12 applicable statutes of the State of Washington and the Refunding Trust Agreement. All necessary
13 and proper fees, compensation and expenses of the Refunding Trustee and all other costs incidental
14 to the setting up of the escrow to accomplish the refunding of the Refunded Bonds and costs related
15 to the issuance and delivery of the Bonds, including bond printing, verification fees, Bond Counsel's
16 fees and other related expenses, shall be paid out of the proceeds of the Bonds.

17 (d) Authorization for Refunding Trust Agreement. To carry out the Refunding Plan provided
18 for by this ordinance, the Director of Finance is authorized and directed to execute and deliver to the
19 Refunding Trustee, in connection with each series of Bonds, a Refunding Trust Agreement in a form
20 that is consistent with this ordinance as approved by the Bond Resolution and that assures that the
21 escrow provided therein and the Bonds are in compliance with the requirements of federal law
22 governing the exclusion of interest on the Bonds from gross income for federal income tax purposes.

23 Section 13. Calls for Redemption of the Refunded Bonds. As a part of the Refunding
24 Plan, the City shall call the Refunded Bonds for redemption on the dates and at the prices set forth in
25 the Bond Resolution. Such calls for redemption of the Refunded Bonds shall be irrevocable after the
26 delivery to the initial purchaser thereof of the applicable series of Bonds. The dates on which the

1 Refunded Bonds are called for redemption shall be the earliest dates on which those bonds may be
2 called for redemption.

3 The proper officials of the City are authorized and directed to give or cause to be given such
4 notices as required, at the times and in the manner required pursuant to the Refunded Bond
5 Ordinance in order to effect the redemption prior to maturity of the Refunded Bonds.

6 Section 14. City Findings with Respect to Refunding. The Refunding Plan, or any portion
7 thereof, shall be carried out only if the City Council finds and determines by the Bond Resolution
8 that the issuance and sale of Bonds will effect savings to the City and its ratepayers and/or otherwise
9 will be in the best interest of the City and in the public interest. In making such findings and
10 determinations, the City Council shall give consideration to the fixed maturities and scheduled
11 redemptions of the Bonds, the costs of issuance of the Bonds and the known earned income from the
12 investment of the proceeds of the issuance and sale of the Bonds and other money, if any, of the City
13 used in the refunding pending payment and redemption of the Refunded Bonds.

14 The Refunding Plan, or any portion thereof, shall be carried out only if the City Council
15 further finds and determines that the money to be deposited with the Bond Registrar for the
16 Refunded Bonds and/or the Refunding Trustee in accordance with this ordinance and the Bond
17 Resolution will discharge and satisfy the obligations of the City with respect to the Refunded Bonds
18 under the Refunded Bond Ordinance, and the pledges, charges, trusts, covenants and agreements of
19 the City therein made or provided for as to the Refunded Bonds, and that the Refunded Bonds shall
20 no longer be deemed to be outstanding under such ordinances immediately upon the deposit of such
21 money.

22 Section 15. City Findings of Sufficiency of Revenues. The Bonds shall be issued only if
23 the City Council finds and determines by the Bond Resolution that the issuance and sale of the
24 Bonds is in the best interest of the City and in the public interest. In making such findings and
25 determinations, the City Council shall give due regard to the cost of operation and maintenance of
26 the Light System and to any portion of the Gross Revenues pledged for the payment of any bonds,

1 warrants or other indebtedness, and shall find and determine that the Gross Revenues, at the rates
2 established from time to time consistent with Section 17(d) of this ordinance, will be sufficient, in
3 the judgment of the City Council, to meet all expenses of operation and maintenance of the Light
4 System and to provide the amounts previously pledged for the payment of all outstanding obligations
5 payable out of the Gross Revenue and pledged herein for the payment of the Bonds.

6 Section 16. Security for the Bonds. The Bonds shall be special limited obligations of the
7 City payable from and secured solely by the Gross Revenues and by money in the Parity Bond Fund
8 and the Reserve Fund. The Gross Revenues are pledged to make the payments into the Parity Bond
9 Fund and the Reserve Fund required by Section 17(a) and (b) of this ordinance, which pledge shall
10 constitute a charge upon such Gross Revenues prior and superior to all other charges whatsoever,
11 save and except reasonable charges for maintenance and operation of the Light System.

12 The Bonds shall not in any manner or to any extent constitute general obligations of the City,
13 the State of Washington or any political subdivision of the State of Washington or a charge upon any
14 general fund or upon any money or other property of the City, the State of Washington or any
15 political subdivision of the State of Washington not specifically pledged thereto by this ordinance.

16 Section 17. Bond Covenants.

17 (a) Parity Bond Fund. A special fund of the City known as the “Seattle Municipal Light
18 Revenue Parity Bond Fund” (the “Parity Bond Fund”) has heretofore been created by
19 Ordinance 92938, and is now maintained as a separate account within the Light Fund, for the sole
20 purpose of paying the principal of and interest on the bonds therein authorized and future bonds
21 issued on a parity therewith as the same shall become due. The Bonds shall be payable, principal,
22 premium, if any, and interest, out of the Parity Bond Fund.

23 From and after the issuance of the Bonds, and so long thereafter as obligations are
24 outstanding against the Parity Bond Fund (including any Payment Agreement Payments required to
25 be made under any Parity Payment Agreements), the Director of Finance shall set aside and pay into
26 the Parity Bond Fund on or prior to the respective dates on which the interest on or principal of and

1 interest on the Bonds shall become due and payable certain fixed amounts out of the Gross Revenues
2 sufficient to pay such interest or principal and interest as the same shall become due.

3 Money in the Parity Bond Fund shall, to the fullest extent practicable and reasonable, be
4 invested and reinvested at the direction of the Director of Finance solely in, and obligations
5 deposited in such accounts shall consist of, Permitted Investments. Earnings on money and
6 investments in the Parity Bond Fund shall be deposited in and used for the purposes of that fund.

7 (b) Reserve Fund. A special fund of the City known as the “Municipal Light and Power
8 Bond Reserve Fund” (the “Reserve Fund”) has heretofore been created by Ordinance 71917, as
9 amended, and is now maintained as a separate account within the Light Fund, for the purpose of
10 securing the payment of the principal of and interest on all Parity Bonds outstanding (including
11 amounts due under any Parity Payment Agreements).

12 The City covenants and agrees that it will pay into the Reserve Fund out of any money
13 legally available therefor, within five (5) years from the date of issuance of the Bonds, the amount
14 required to fund the Reserve Fund to the Reserve Fund Requirement.

15 Money held in the Reserve Fund shall, to the fullest extent practicable and reasonable, be
16 invested and reinvested at the direction of the Director of Finance solely in, and obligations
17 deposited in such accounts shall consist of, Permitted Investments. Earnings on money and
18 investments in the Reserve Fund shall be deposited in that fund and credited against amounts
19 required to be deposited therein until the Reserve Fund is fully funded, and thereafter such earnings
20 shall be deposited in the Parity Bond Fund.

21 (i) Reserve Fund Requirement.

22 (A) The City shall provide in the Parity Bond Ordinance authorizing the
23 issuance of any Future Parity Bonds for deposit into the Reserve Fund out of the Gross Revenues (or
24 out of any other funds of the City on hand and legally available therefor, including the proceeds of
25 the Future Parity Bonds being issued or any other Future Parity Bonds) of periodic payments so that
26 by five (5) years from the date of such Future Parity Bonds there will have been paid into the

1 Reserve Fund an amount which, together with the money already on deposit therein, will be at least
2 equal to the Reserve Fund Requirement for all Parity Bonds outstanding at the end of that five-year
3 period.

4 (B) Notwithstanding the foregoing, any Parity Bond Ordinance may provide
5 for the City to obtain Qualified Insurance or a Qualified Letter of Credit for specific amounts
6 required to be paid into the Reserve Fund. The amount available to be drawn upon under such
7 Qualified Insurance or Qualified Letter of Credit shall be credited against the amounts required to be
8 maintained in the Reserve Fund by Section 17(b)(i)(A).

9 (C) Such Qualified Letter of Credit or Qualified Insurance shall not be
10 cancelable on less than five (5) years' notice. In the event of receipt of any such notice of
11 cancellation, the City shall substitute Qualified Insurance or a Qualified Letter of Credit in the
12 amount required pursuant to Section 17(b)(i)(A) or in the alternative shall create a special account in
13 the Light Fund and deposit therein, on or before the twenty-fifth (25th) day of each of the sixty
14 (60) succeeding calendar months, one sixtieth (1/60th) of the amount sufficient, together with other
15 money and investments on deposit in the Reserve Fund, to equal the Reserve Fund Requirement on
16 the date any such cancellation shall become effective. Such amounts shall be transferred from
17 money in the Light Fund (after making provision for payment of operating and maintenance
18 expenses and for the required payments into the Parity Bond Fund). Amounts on deposit in such
19 special account shall not be available to pay debt service on Parity Bonds or for any other purpose of
20 the City, and shall be transferred to the Reserve Fund on the effective date of any cancellation of a
21 Qualified Letter of Credit or Qualified Insurance to make up the deficiency caused thereby.

22 (D) If the amount in the Reserve Fund shall be less than the Reserve Fund
23 Requirement (taking into account the five (5) year period referred to in Section 17(b)(i)(A)), the City
24 shall transfer to the Reserve Fund money in an amount sufficient to restore the Reserve Fund to the
25 Reserve Fund Requirement within twelve (12) months after the date of such deficiency. The City
26 shall transfer such amounts first from money in the Light Fund (after making provision for payment

1 of operating and maintenance expenses and for the required payments into the Parity Bond Fund)
2 and only thereafter from money in any construction fund or account established with respect to any
3 issue of Parity Bonds, first taking money from the unrestricted portion thereof, then taking money
4 from the restricted portion thereof. If the amount in the Reserve Fund shall be greater than the
5 Reserve Fund Requirement, then and only then may the City withdraw such excess from the Reserve
6 Fund and deposit such excess in the Light Fund.

7 (ii) Use of Reserve Fund for Refunding Bonds. If any Parity Bonds are refunded,
8 the money set aside in the Reserve Fund to secure the payment of such Parity Bonds may be used to
9 retire such Parity Bonds or may be transferred to any reserve fund or account which may be created
10 to secure the payment of any bonds issued to refund such Parity Bonds, as long as the money left
11 remaining in the Reserve Fund is at least equal, together with any Qualified Insurance or Qualified
12 Letters of Credit, to the Reserve Fund Requirement.

13 (iii) Use of Reserve Fund for Payment of Debt Service. If the money in the Parity
14 Bond Fund is insufficient to meet maturing installments of either interest on or principal of and
15 interest on the Parity Bonds payable out of the Parity Bond Fund (including amounts payable under
16 any Parity Payment Agreements), such deficiency shall be made up from the Reserve Fund by the
17 withdrawal of money or proceeds of Qualified Insurance or Qualified Letters of Credit therefrom, as
18 the case may be. Any deficiency created in the Reserve Fund by reason of any such withdrawal or
19 claim against Qualified Insurance or a Qualified Letter of Credit shall then be made up out of the
20 Gross Revenues (or out of such other funds of the City on hand and legally available therefor), after
21 making necessary provision for the payments required to be made for operation and maintenance of
22 the Light System and debt service on any obligations payable from such Gross Revenues.

23 (iv) Withdrawals From Reserve Fund. Money in the Reserve Fund may be
24 withdrawn by the City for any lawful purpose as long as the aggregate of any money, Qualified
25 Insurance and Qualified Letters of Credit left remaining on deposit in the Reserve Fund is at least
26 equal to the Reserve Fund Requirement for the Parity Bonds then outstanding.

1 The City reserves the right to substitute Qualified Insurance or a Qualified Letter of Credit
2 for money previously deposited in the Reserve Fund and to withdraw such money to the extent
3 described in the preceding paragraph.

4 Any withdrawals from subaccounts within the Reserve Fund shall be made on a pro rata
5 basis except when the provider of a Qualified Letter of Credit or Qualified Insurance requires all
6 cash and investments in the Reserve Fund to be withdrawn before draws on the Qualified Letter of
7 Credit or Qualified Insurance, or unless the City receives an opinion of Bond Counsel to the effect
8 that such pro rata withdrawal is not required to maintain the exclusion of interest on the Parity Bonds
9 then outstanding from gross income.

10 (c) Sale or Disposition of the Light System.

11 (i) The City may dispose of all or substantially all of the Light System if the City
12 simultaneously causes all of the Parity Bonds to be, or deemed to be, no longer outstanding.

13 (ii) Except as provided below, the City will not dispose of any part of the Light
14 System in excess of 5% of the value of the net utility plant of the Light System in service unless
15 prior to such disposition:

16 (A) there has been filed with the Director of Finance a certificate of the
17 Professional Utility Consultant stating that such disposition will not impair the ability of the City to
18 comply with the rate covenant set forth in Section 17(d); or

19 (B) provision is made for the payment, redemption or other retirement of a
20 principal amount of Parity Bonds equal to the greater of the following amounts:

21 (I) An amount which will be in the same proportion to the net
22 principal amount of Parity Bonds then outstanding (defined as the total principal amount of Parity
23 Bonds then outstanding less the amount of cash and investments in the Parity Bond Fund) that the
24 Gross Revenues for the twelve (12) preceding months attributable to the part of the Light System
25 sold or disposed of bears to the total Gross Revenues for such period; or
26

1 (II) An amount which will be in the same proportion to the net
2 principal amount of Parity Bonds then outstanding that the book value of the part of the Light
3 System sold or disposed of bears to the book value of the entire Light System immediately prior to
4 such sale or disposition.

5 (iii) The City may dispose of any portion of the Light System that has become
6 unserviceable, inadequate, obsolete, worn out or unfit to be used or no longer necessary, material to
7 or useful in the operation of the Light System.

8 (iv) If the ownership of all or part of the Light System is transferred from the City
9 through the operation of law, the City shall reconstruct or replace the transferred portion using any
10 proceeds of the transfer unless the City Council determines that such reconstruction or replacement
11 is not in the best interests of the City and the owners of the Parity Bonds, in which case any proceeds
12 shall be used to retire Parity Bonds prior to maturity.

13 (d) Rates and Charges. The City will establish from time to time and maintain such rates for
14 electric energy as will maintain the Light System in sound financial condition and provide sufficient
15 revenues to permit the payment of sums into the special fund which the City has pledged to be set
16 aside for the payment of principal and interest, as herein provided, to be applied to the payment of
17 the principal of and interest on the Parity Bonds until the Parity Bonds shall have been paid in full,
18 and in addition thereto, will pay all costs of operation and maintenance, and all bonds, warrants and
19 indebtedness for which any revenues of the Light System shall have been heretofore pledged.

20 (e) Maintenance and Operation of the Light System. The City will operate the properties of
21 the Light System in an efficient manner and at a reasonable cost; and will maintain, preserve and
22 keep, or cause to be maintained, preserved and kept, the properties of the Light System and every
23 part and parcel thereof in good repair, working order and condition; and from time to time will make
24 or cause to be made all necessary and proper repairs, renewals and replacements thereto so that at all
25 times the business carried on in connection therewith will be properly and advantageously
26 conducted.

1 (f) Books and Financial Statements. The City will keep and maintain proper books of
2 account for the Light System in accordance with generally accepted accounting principles applicable
3 to governmental utilities, and will generally adhere to the uniform system of accounts prescribed by
4 the Division of Municipal Corporations of the State Auditor's Office and the Federal Energy
5 Regulatory Commission; and will prepare, on or before one hundred twenty (120) days after each
6 calendar year, annual financial statements showing reasonable detail, including a balance sheet, an
7 income statement and a statement of cash flows or other such statement. Copies of such financial
8 statements shall be placed on file in the office of the Director of Finance and shall be open to
9 inspection at any reasonable time by any owner (or beneficial owner) of any Parity Bonds. A copy
10 of such financial statements shall be sent to any owner (or beneficial owner) of Parity Bonds, upon
11 request in writing setting forth the name and address to which such financial statements may be sent.

12 (g) Issuance of Future Parity Bonds. Except as provided in Section 17(h) of this ordinance
13 for the issuance of Refunding Parity Bonds, Future Parity Bonds may be issued (and Parity Payment
14 Agreements may be entered into), from time to time in one or more series for any lawful purpose of
15 the City's Light Department, only if at the time of the delivery of each series of Future Parity Bonds
16 to the initial purchasers thereof (or on the effective date of the Parity Payment Agreement):

17 (i) There is no deficiency in the Parity Bond Fund or in any of the accounts
18 therein and provision has been made to meet the Reserve Fund Requirement for all Parity Bonds
19 then outstanding plus such proposed series of Parity Bonds; and

20 (ii) There shall have been filed with the City either:

21 (A) a certificate of the Director of Finance stating that Net Revenue in any
22 twelve (12) consecutive months out of the most recent twenty-four (24) months preceding the
23 delivery of the Parity Bonds then proposed to be issued (the "Base Period") was not less than one
24 hundred twenty-five percent (125%) of maximum Annual Debt Service in any future calendar year
25 on all Parity Bonds then outstanding and the Parity Bonds then proposed to be issued (except that if
26 any adjustment in the rates, fees and charges for the services of the Light System shall be effective at

1 any time on or prior to the date of delivery of the Parity Bonds then proposed to be issued or within
2 six (6) months after the delivery of such Parity Bonds, the Director of Finance shall reflect in his or
3 her certificate the Net Revenue he or she calculates would have been collected in the Base Period if
4 such new rates, fees and charges had been in effect for the entire Base Period), or

5 (B) a certificate of the Professional Utility Consultant setting forth:

6 (I) the amount of the Adjusted Net Revenue computed as
7 provided in paragraph (C) below;

8 (II) the amount of maximum Annual Debt Service in any calendar
9 year thereafter on account of all Parity Bonds to be outstanding in such calendar year, including the
10 Parity Bonds proposed to be issued, and stating that the amount shown in paragraph (B)(I) above is
11 not less than one hundred twenty-five percent (125%) of the amount shown in this paragraph (B)(II).

12 “Net Revenue” as used in this Section 17(g) means that amount determined by deducting
13 from the Gross Revenues the expenses of operation, maintenance and repair of the Light System,
14 *except that on the New Covenant Date, “Net Revenue” as used in this Section 17(g) shall mean that*
15 *amount determined by deducting from the Gross Revenues the expenses of operation, maintenance*
16 *and repair of the Light System and further deducting any deposits into the Rate Stabilization*
17 *Account, and by adding to Gross Revenues any withdrawals from the Rate Stabilization Account..*

18 (iii) For the purposes of the certificate required by paragraph (ii) above, Adjusted
19 Net Revenue shall be computed by the Professional Utility Consultant as follows:

20 The Net Revenue for the Base Period shall be adjusted by any or all of the following
21 conditions and requirements as may be appropriate to the circumstances:

22 (A) If the Parity Bonds are being issued for the purpose of acquiring operating
23 electric utility properties having an earnings record, the Professional Utility Consultant shall
24 estimate the effect on the Net Revenue for the Base Period of the acquisition of such electric utility
25 properties and the integration thereof into the Light System, and shall adjust the Net Revenue for the
26 Base Period to give effect to such estimate. Any such estimate shall be based upon the operating

1 experience and records of the City and upon any available financial statements and records relating
2 to the earnings of such electric utility properties to be acquired.

3 (B) If any changes have been adopted by the City Council and are in effect on
4 the date of sale of the Parity Bonds or are to go into effect not later than twelve (12) months after
5 such date, in any rates and charges imposed by the City on sales of power and energy and other
6 services furnished by the Light System which were not in effect during the entire Base Period, the
7 Professional Utility Consultant may, if such changes resulted in increases in such rates and charges,
8 and shall, if such changes resulted in reductions in such rates and charges, adjust the Net Revenue
9 for the Base Period to reflect any change in such Net Revenue which would have occurred if the
10 changed rates and charges had been in effect during the entire Base Period.

11 (C) If the purpose for which the Parity Bonds are being issued is to acquire or
12 construct generation or transmission facilities required to furnish or make available to the Light
13 System additional power and energy, or transmission facilities required to enable the City to sell
14 additional power and energy, the Professional Utility Consultant may adjust the Net Revenue for the
15 Base Period by (a) deducting the amount of the estimated increase in Operating Expenses resulting
16 from the acquisition or construction of such facilities in their first year of full operation, (b) adding
17 any additional revenues to be derived from the sale or transmission of such additional power and
18 energy pursuant to executed power sales contracts, and (c) adding an amount equal to the estimated
19 cost of the power and energy which would have been replaced or displaced by such facilities had
20 such additional power and energy in excess of the power and energy to be sold pursuant to clause
21 (b) above been used in the Light System during the Base Period.

22 (D) If there were any customers added to the Light System during the Base
23 Period or thereafter and prior to the date of the Professional Utility Consultant's certificate, the Net
24 Revenue may be adjusted on the basis that such added customers were customers of the Light
25 System during the entire Base Period.

1 (E) If extensions of or additions to the Light System (not described in
2 subparagraph (C) above) are in the process of construction on the date of the Professional Utility
3 Consultant's certificate, or if the proceeds of the Parity Bonds being issued are to be used to acquire
4 or construct extensions of or additions to the Light System (not described in subparagraph
5 (C) above), the Net Revenue for the Base Period may be adjusted by adding any additional revenues
6 not included in the preceding paragraphs that will be derived from such additions and extensions and
7 deducting the estimated increase in operating and maintenance expenses resulting from such
8 additions and extensions.

9 (F) The Net Revenue for the Base Period may be adjusted by excluding from
10 the determination of expenses of operation, maintenance and repair of the Light System any
11 extraordinary, nonrecurring expenses of the Light System or any judgments or amounts to be paid in
12 settlement of claims against the Light System.

13 (iv) In rendering any certificate under this Section 17(g), the Professional Utility
14 Consultant may rely upon, and such certificate shall have attached thereto, (A) financial statements
15 of the Light System, certified by the Director of Finance, showing income and expenses for the
16 period upon which the same are based and a balance sheet as of the end of such period, (B) similar
17 certified statements by the Division of Municipal Corporations of the Office of the State Auditor of
18 the State (or any successor thereto), or (C) similar certified statements by a Certified Public
19 Accountant for as much of such period as any examination by them has been made and completed.
20 If two or more of such statements are inconsistent with each other, the Professional Utility
21 Consultant shall rely on the statement described under clause (A) in this Section 17(g)(iv).

22 (h) Issuance of Refunding Parity Bonds.

23 (i) Without complying with the provisions of Section 17(g) of this ordinance, the
24 City may at any time and from time to time issue one or more series of Refunding Parity Bonds, but
25 only if there shall have been filed with the City a certificate of the Director of Finance stating that
26 Annual Debt Service immediately after the issuance of such Refunding Parity Bonds (calculated by

1 including debt service on the Refunding Parity Bonds but excluding debt service on the bonds to be
2 refunded with the proceeds thereof) does not exceed the Annual Debt Service immediately prior to
3 the issuance of the Refunding Parity Bonds (calculated by including debt service on the bonds to be
4 refunded but excluding debt service on the Refunding Parity Bonds) by more than Five Thousand
5 dollars (\$5,000) in any calendar year that any then-outstanding Parity Bonds are anticipated to be
6 outstanding.

7 (ii) Parity Bonds of any one or more series or one or more maturities within a
8 series may be refunded by a single series of Refunding Parity Bonds, which Parity Bonds to be
9 refunded shall be specified in the Parity Bond Ordinance providing for the issuance of the Refunding
10 Parity Bonds, and the principal amount of such Refunding Parity Bonds may include amounts
11 necessary to pay the principal of the Parity Bonds to be refunded, interest thereon to the date of
12 payment or redemption thereof, any premium payable thereon upon such payment or redemption and
13 the costs of issuance of such Refunding Parity Bonds. The proceeds of the Refunding Parity Bonds
14 shall be held and applied in such manner as is provided in the Parity Bond Ordinance providing for
15 the issuance of such Refunding Parity Bonds, so that upon the delivery of such Refunding Parity
16 Bonds the Parity Bonds to be refunded thereby shall be deemed to be no longer outstanding in
17 accordance with the provisions of the Parity Bond Ordinance providing for the issuance of those
18 bonds.

19 (iii) Refunding Parity Bonds may also be issued upon compliance with the
20 provisions of Section 17(g) of this ordinance.

21 (iv) Nothing contained in this ordinance shall prohibit or prevent, or be deemed or
22 construed to prohibit or prevent, the City from issuing Refunding Parity Bonds to fund or refund
23 maturing Parity Bonds of the City for the payment of which money is not otherwise available.

24 Section 18. Preservation of Tax Exemption for Interest on Bonds. The City covenants
25 that it will take all actions consistent with the terms of the Bonds, this ordinance and the Bond
26 Resolution, reasonably within its power and necessary to prevent interest on the Bonds from being

1 included in gross income for federal income tax purposes, and it will neither take any action nor
2 make or permit any use of proceeds of the Bonds or other funds of the City treated as proceeds of the
3 Bonds at any time during the term of the Bonds which will cause interest on the Bonds to be
4 included in gross income for federal income tax purposes.

5 The City has not been notified of any listing or proposed listing by the Internal Revenue
6 Service to the effect that it is a bond issuer whose arbitrage certifications may not be relied upon.

7 Section 19. Advance Refunding or Defeasance of Bonds. The City may issue advance
8 refunding bonds pursuant to the laws of the State or use money available from any other lawful
9 source to pay when due the principal of and premium, if any, and interest on the Bonds, or any
10 portion thereof included in a refunding or defeasance plan, and to redeem and retire, release, refund
11 or defease those Bonds (the “Defeased Bonds”) and to pay the costs of such refunding or defeasance.
12 If money and/or Government Obligations sufficient in amount, together with known earned income
13 from the investments thereof, to redeem and retire, release, refund or defease the Defeased Bonds in
14 accordance with their terms, are set aside in a special trust fund or escrow account irrevocably
15 pledged to that redemption, retirement or defeasance (the “Trust Account”), then all right and
16 interest of the owners of the Defeased Bonds in the covenants of this ordinance and in the Gross
17 Revenue and the funds and accounts pledged to the payment of the Defeased Bonds, other than the
18 right to receive the funds so set aside and pledged, thereafter shall cease and become void. Such
19 owners thereafter shall have the right to receive payment of the principal of and interest or
20 redemption price on the Defeased Bonds from the Trust Account. The City shall include in the
21 refunding or defeasance plan such provisions as the City deems necessary for the random selection
22 of any Defeased Bonds that constitute less than all of a particular maturity of the Bonds, for notice of
23 the defeasance to be given to the owners of the Defeased Bonds and to such other persons as the City
24 shall determine, and for any required replacement of Bond certificates for defeased Bonds.

25 After the establishing and full funding of such a Trust Account, the Defeased Bonds shall be
26 deemed no longer outstanding and the City may apply any money in any other fund or account

1 established for the payment or redemption of the Defeased Bonds to any lawful purposes as it shall
2 determine, subject only to the rights of the owners of any other Parity Bonds.

3 If the refunding plan provides that the Defeased Bonds be secured by money and/or
4 Government Obligations pending the prior redemption of the Defeased Bonds and if such refunding
5 plan also provides that certain money and/or Government Obligations are pledged irrevocably for
6 the prior redemption of the Defeased Bonds included in that refunding plan, then only the debt
7 service on the Bonds which are not Defeased Bonds and the refunding bonds, the payment of which
8 is not so secured by the refunding plan, shall be included in the computation of the coverage
9 requirement for the issuance of Future Parity Bonds and for determining compliance with rate
10 covenants.

11 Section 20. Amendments.

12 (a) Amendments Without Bond Owners' Consent. The City Council from time to time and
13 at any time may pass a resolution or resolutions, or ordinance or ordinances, supplemental hereto,
14 which resolution or resolutions, ordinance or ordinances thereafter shall become a part of this
15 ordinance, for any one or more of the following purposes:

16 (i) To add to the covenants and agreements of the City contained in this
17 ordinance other covenants and agreements thereafter to be observed which shall not adversely affect
18 the interests of the owners of any Parity Bonds then outstanding, or to surrender any right or power
19 herein reserved to or conferred upon the City.

20 (ii) To make such provisions for the purpose of curing any ambiguities or of
21 curing, correcting or supplementing any defective provision contained in this ordinance in regard to
22 matters or questions arising under this ordinance as the City Council may deem necessary or
23 desirable and not inconsistent with this ordinance and which shall not adversely affect the interests
24 of owners of any Parity Bonds then outstanding in any material respect.

25 (iii) To make such changes as are necessary to permit the Bonds to be held in
26 registered certificate form or in fully immobilized form by a Securities Depository other than DTC.

Any such supplemental resolution or ordinance of the City may be passed without the consent of the owners of any Parity Bonds at any time outstanding, notwithstanding any of the provisions of Section 20(b) of this ordinance, but only upon receipt by the City of an opinion of Bond Counsel to the effect that the amendment is permitted by the terms of this ordinance. The City shall deliver a copy of any such supplemental resolution or ordinance to Moody's, S&P or any other rating agency then maintaining a rating on any Parity Bonds then outstanding prior to its passage by the City.

(b) Amendments With Bond Owners' Consent. The City Council may, with the consent of the owners of not less than sixty percent (60%) in aggregate principal amount of the Parity Bonds then outstanding, pass a resolution or resolutions or ordinance or ordinances supplemental hereto for the purpose of adding any provisions to or changing in any manner or eliminating any of the provisions of this ordinance or of any supplemental resolution or ordinance, except no such supplemental resolution or ordinance shall:

(i) Extend the fixed maturity of any Parity Bonds, or reduce the rate of interest thereon, or extend the times of payment of interest from their respective due dates, or reduce the amount of the principal thereof, or reduce any premium payable on the redemption thereof, without the consent of the owner of each Parity Bond so affected; or

(ii) Reduce the aforesaid percentage of bond owners required to approve any such supplemental resolution or ordinance, without the consent of the owners of all of the Parity Bonds then outstanding.

For purposes of determining whether the owners of the requisite percentage of principal amount of Parity Bonds have consented to any amendment to this ordinance, the Accreted Value of Capital Appreciation Bonds shall be deemed to be the principal amount thereof.

It shall not be necessary for the consent of bond owners under this Section 20(b) to approve the particular form of any proposed supplemental ordinance or resolution, but it shall be sufficient if such consent shall approve the substance thereof.

1 (c) Effect of Amendment. Upon the passage of any supplemental resolution or ordinance
2 pursuant to the provisions of this section, this ordinance shall be deemed to be modified and
3 amended in accordance therewith, and the respective rights, duties and obligations of the City under
4 this ordinance shall thereafter be determined, exercised and enforced thereunder, subject in all
5 respects to such modification and amendments, and all the terms and conditions of any such
6 supplemental resolution or ordinance shall be deemed to be a part of the terms and conditions of this
7 ordinance for any and all purposes.

8 (d) Notation on Bonds. Parity Bonds executed and delivered after the execution of any
9 supplemental resolution or ordinance passed pursuant to the provisions of this Section 20 may have a
10 notation as to any matter provided for in such supplemental resolution or ordinance, and if such
11 supplemental resolution or ordinance shall so provide, new bonds modified to conform, in the
12 opinion of the City Council, to any modification of this ordinance contained in any such
13 supplemental resolution or ordinance may be prepared by the City and delivered without cost to the
14 owners of any affected Parity Bonds then outstanding, upon surrender for cancellation of such bonds
15 in equal aggregate principal amounts.

16 Section 21. Rate Stabilization Account. There is hereby established in the Light Fund a
17 Rate Stabilization Account. On the New Covenant Date, the City may at any time deposit in the
18 Rate Stabilization Account, Gross Revenue and any other money received by the Light System and
19 available to be used therefor. Thereafter, the City may withdraw any or all of the money from the
20 Rate Stabilization Account for inclusion in the Net Revenue for any fiscal year of the City. Such
21 deposits or withdrawals may be made up to and including the date ninety (90) days after the end of
22 the fiscal year for which the deposit or withdrawal will be included as Net Revenue.

23 Section 22. Sale of Bonds. The Director of Finance may provide for the sale of the Bonds
24 by public sale or by a negotiated sale, limited offering or private placement, with the successful
25 underwriter, placement agent or purchaser, as applicable, chosen through a selection process
26 acceptable to the Director of Finance. The terms of that sale, which may include a forward or

1 delayed delivery of the Bonds, shall be consistent with this ordinance and the Bond Resolution, and
2 shall be confirmed by the Bond Resolution. The Bonds will be delivered to the purchasers as
3 provided in the Bond Resolution, immediately upon payment to the City of the purchase price plus
4 accrued interest to the date of closing in immediately available federal funds in Seattle, Washington,
5 at the City's expense or at another place upon which the Director of Finance and the purchaser may
6 mutually agree at the purchaser's expense.

7 CUSIP numbers (if required) will be printed on the Bonds, but neither failure to print CUSIP
8 numbers on any Bond nor error with respect thereto shall constitute cause for a failure or refusal by
9 the purchasers to accept delivery of and pay for the Bonds in accordance with the purchase offer.
10 All expenses in relation to the printing of CUSIP numbers on the Bonds shall be paid by the City,
11 but the fee of the CUSIP Service Bureau for the assignment of those numbers shall be the
12 responsibility of and shall be paid by the purchasers.

13 The City will cause the Bonds to be typed, photocopied, printed or lithographed, sealed and
14 executed and will furnish the approving legal opinion of Bond Counsel regarding the Bonds, the
15 opinion also being printed on each Bond unless the Bond is typed or photocopied.

16 Section 23. Continuing Disclosure. The City shall undertake to provide for the benefit of
17 holders of the Bonds disclosure of certain financial information and operating data of the type
18 included in the final official statement, if any, for the Bonds, as well as disclosure of certain material
19 events respecting the Bonds, in the manner and to the extent required by United States Securities and
20 Exchange Commission Rule 15c2-12. The particular terms of the undertaking shall be set forth in
21 the Bond Resolution.

22 Section 24. General Authorization. The Mayor and the Director of Finance and each of
23 the other appropriate officers of the City are each authorized and directed to do everything as in their
24 judgment may be necessary, appropriate or desirable in order to carry out the terms and provisions
25 of, and complete the transactions contemplated by, this ordinance. In particular, and without
26 limitation, the Director of Finance may, in his discretion and without further action by the City

1 Council, (a) comply with any continuing disclosure requirements applicable to the Bonds, (b) deem
2 final and approve the distribution of the preliminary official statement prepared in connection with
3 the sale of the Bonds, and (c) change the Bond Registrar or Securities Depository for the Bonds.

4 Section 25. Severability. The provisions of this ordinance are declared to be separate and
5 severable. If a court of competent jurisdiction, all appeals having been exhausted or all appeal
6 periods having run, finds any provision of this ordinance to be invalid or unenforceable as to any
7 person or circumstance, such offending provision shall, if feasible, be deemed to be modified to be
8 within the limits of enforceability or validity. However, if the offending provision cannot be so
9 modified, it shall be null and void with respect to the particular person or circumstance, and all other
10 provisions of this ordinance in all other respects, and the offending provision with respect to all other
11 persons and all other circumstances, shall remain valid and enforceable.

12 Section 26. Ratification of Prior Acts. Any action taken consistent with the authority but
13 prior to the effective date of this ordinance, including, if applicable, but not limited to giving notices
14 of the sale of Bonds, selecting an underwriter or placement agent for the Bonds, adopting the Bond
15 Resolution, executing contracts, making fund transfers and paying warrants, is ratified, approved and
16 confirmed.

17 Section 27. Headings. Section headings in this ordinance are used for convenience only
18 and shall not constitute a substantive portion of this ordinance.

APPENDIX B

FORM OF BOND COUNSEL OPINION

(This page intentionally left blank.)



FORM OF BOND COUNSEL OPINION

The City of Seattle, Washington

Re: The City of Seattle, Washington, \$251,850,000 Municipal Light and Power Improvement and Refunding Revenue Bonds, 2003

We have served as bond counsel to The City of Seattle, Washington (the "City"), in connection with the issuance of the above-referenced bonds (the "Bonds"), and in that capacity have examined such law and such certified proceedings and other documents as we have deemed necessary to render this opinion. As to matters of fact material to this opinion and of which attorneys within the firm involved with the issuance of the Bonds have no independent knowledge, we have relied upon representations contained in the certified proceedings and other certifications of public officials furnished to us.

The Bonds are issued pursuant to the laws of the State of Washington and Ordinance 121198 and Resolution 30618 of the City (collectively, the "Bond Legislation") to provide all or part of the funds to pay part of the cost of the Plan of Additions, to pay the costs of refunding the Refunded Bonds and to pay the costs of issuance and sale of the Bonds, all as set forth in the Bond Legislation.

Reference is made to the Bond Legislation for the definitions of the capitalized terms used and not otherwise defined herein.

The Bonds are special limited obligations of the City payable from and secured solely by the Gross Revenues of the Light System and by money in the Seattle Municipal Light Revenue Parity Bond Fund (the "Parity Bond Fund") and the Municipal Light and Power Bond Reserve Fund (the "Reserve Fund"). The Gross Revenues have been pledged to make the required payments into the Parity Bond Fund and the Reserve Fund, which pledge constitutes a charge on the Gross Revenues prior and superior to all other charges whatsoever, except reasonable charges for maintenance and operation of the Light System, and except that the Bonds shall have a lien and charge upon such Gross Revenues on a parity with the lien and charge of the Outstanding Parity Bonds and any Future Parity Bonds.

1111 THIRD
AVENUE
Suite 3400
SEATTLE
Washington
98101-3299

Telephone
(206) 447-4400
Facsimile
(206) 447-9700
Website
WWW.FOSTER.COM

ANCHORAGE
Alaska

PORTLAND
Oregon

SEATTLE
Washington

SPOKANE
Washington

Under the Internal Revenue Code of 1986, as amended (the "Code"), the City is required to comply with certain requirements after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Bond proceeds and the facilities financed or refinanced with Bond proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances and the arbitrage rebate requirement to the extent applicable to the Bonds. The City has covenanted in the Bond Legislation to comply with those requirements, but if the City fails to comply with those requirements, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds. We have not undertaken and do not undertake to monitor the City's compliance with such requirements.

As of the date of initial delivery of the Bonds to the purchaser thereof and full payment therefor, it is our opinion that under existing law:

1. The City is a duly organized and legally existing first class city under the laws of the State of Washington;

2. The City has duly authorized and approved the Bond Legislation, and the Bonds have been duly authorized and executed by the City and are issued in full compliance with the provisions of the Constitution and laws of the State of Washington, the Bond Legislation and other ordinances and resolutions of the City relating thereto;

3. The Bonds constitute valid and binding obligations of the City payable solely out of the Gross Revenues of the Light System and money in the Parity Bond Fund and the Reserve Fund, except only to the extent that enforcement of payment may be limited by bankruptcy, insolvency or other laws affecting creditors' rights and principles of equity if equitable remedies are sought;

4. The Bonds are not general obligations of the City; and

5. Assuming compliance by the City after the date of issuance of the Bonds with applicable requirements of the Code, the interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals; however, while interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by corporations is to be taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by certain S corporations may be subject to tax, and interest on the Bonds received by foreign corporations with United States branches may be subject to a foreign branch profits tax. We express no opinion regarding any other federal tax consequences of receipt of interest on the Bonds.

The City of Seattle, Washington
_____, 2003

This opinion is given as of the date hereof, and we assume no obligation to revise or supplement this opinion to reflect any facts or circumstances that may hereafter come to our attention, or any changes in law that may hereafter occur.

We express no opinion herein concerning the completeness or accuracy of any official statement, offering circular or other sales or disclosure material relating to the issuance of the Bonds or otherwise used in connection with the Bonds.

We bring to your attention the fact that the foregoing opinions are expressions of our professional judgment on the matters expressly addressed and do not constitute guarantees of result.

Respectfully submitted,

FOSTER PEPPER & SHEFELMAN PLLC

(This page intentionally left blank.)

APPENDIX C

2002 AUDITED FINANCIAL STATEMENTS OF THE DEPARTMENT

(This page intentionally left blank.)

***City of Seattle –
City Light Department***

*Financial Statements for the
Years Ended December 31, 2002 and 2001, and
Independent Auditors' Report*

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITORS' REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	2 – 10
FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2002 AND 2001:	
Balance Sheets	11
Statements of Revenues, Expenses, and Changes in Equity	12
Statements of Cash Flows	13 – 14
Notes to Financial Statements	15 – 35



INDEPENDENT AUDITORS' REPORT

Superintendent
City of Seattle – City Light Department
Seattle, Washington

We have audited the accompanying balance sheets of the City of Seattle – City Light Department (the “Department”) as of December 31, 2002 and 2001, and the related statements of revenues, expenses, and changes in equity and of cash flows for the years then ended. These financial statements are the responsibility of the Department’s management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Department as of December 31, 2002 and 2001, and the changes of its equity and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1 to the financial statements, in fiscal year 2002, the Department adopted Governmental Accounting Standards Board (“GASB”) Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*; GASB Statement No. 37, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments: Omnibus—an Amendment of GASB Statements No. 21 and No. 34*; and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*.

The management’s discussion and analysis on pages 2 through 10 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Deloitte & Touche LLP

April 18, 2003

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

MANAGEMENT’S DISCUSSION AND ANALYSIS DECEMBER 31, 2002

The following discussion and analysis of the financial performance of the City of Seattle – City Light Department (the “Department”) provides a summary of the financial activities for the year ended December 31, 2002. This discussion and analysis should be read in combination with the Department’s financial statements, which immediately follow this section.

RESULTS OF OPERATIONS

Condensed Revenues and Expenses

Year ending December 31,	2002	2001
Operating revenues	\$ 709,330,439	\$ 632,453,970
Nonoperating revenues	<u>10,467,972</u>	<u>13,275,220</u>
Total revenues	719,798,411	645,729,190
Operating expenses	650,574,759	657,656,814
Nonoperating expenses	<u>84,057,713</u>	<u>76,708,493</u>
Total expenses	734,632,472	734,365,307
Capital contributions	10,631,017	12,489,627
Grants and transfers	<u>2,337,759</u>	<u>2,806,083</u>
Net loss	<u>\$ (1,865,285)</u>	<u>\$ (73,340,407)</u>

The Department recorded a net loss of \$1.9 million in 2002, compared with a net loss of \$73.3 million in 2001. Financial results in 2001 reflected the deferral of \$300.0 million in power costs incurred in that year; in 2002 \$100.0 million of the deferred power costs were amortized. Without the deferral and amortization of power costs, the net loss in 2001 would have been \$373.3 million, and net income of \$98.1 million would have been realized in 2002.

The improvement in the Department’s financial results from 2001 to 2002 was heavily influenced by increases in retail rates that were enacted in 2001, the return of more normal water conditions to the Northwest region following the 2000 – 2001 drought, and the availability of additional power through purchased power contracts. As a result of these resource acquisitions and favorable water conditions, the Department generated substantial revenue from the sale of surplus power in the wholesale market.

OPERATING REVENUES

Operating revenues totalled \$709.3 million in 2002, an increase of \$76.9 million, or 12.2%, from the prior year. Significant increases were recorded in both retail and wholesale revenues. These increases were partially offset by a net decrease in other power-related revenues.

Revenue from the sale of power to retail customers in the Department’s service area increased from \$503.4 million in 2001 to \$562.4 million in 2002, an increase of \$59.0 million, or 11.7%. The increase in revenue is attributable to the rate increases that were implemented in stages in 2001 and that were in effect throughout

2002, with only minor adjustments. Rates for nonresidential customers in the downtown network area were increased in March 2002. Rates for all classes were lowered by an average of 1.1% on April 1, 2002, to pass through decreases in the power rates charged by the Bonneville Power Administration (“Bonneville”). The volume of energy sold in 2002 was actually 0.8% lower in 2002 than in 2001, due to the effects of warm winter temperatures and high rates.

Revenue from the sale of surplus energy in the wholesale market increased from \$73.9 million in 2001 to \$112.8 million in 2002, due to a large increase in the volume of energy sold. Energy sold in the wholesale market increased from 468,827 megawatt hours (“MWh”) in 2001 to 4,647,945 MWh in 2002; however, the average price realized on these sales declined sharply, from \$157.63 per MWh in 2001 to \$24.27 in 2002. The result of these two offsetting changes was an increase of \$38.9 million, or 52.6%, in wholesale revenue. Wholesale purchases are discussed below in the section dealing with power and transmission costs.

Other power-related revenues declined from \$44.3 million in 2001 to \$21.1 million in 2002, a decrease of \$23.2 million. The value of energy delivered to other utilities under exchange agreements decreased from \$31.7 million in 2001 to \$5.3 million in 2002. Exchanged energy is valued at the blended weighted-average cost of power to the Department for the periods when the exchanges take place. This value declined sharply from 2001 to 2002. In addition, the amount of energy delivered under exchange agreements was lower in 2002. Similarly, the value of energy delivered under basis transactions declined from \$6.9 million in 2001 to \$2.2 million in 2002, reflecting both a decrease in deliveries and a lower unit value per MWh delivered. Revenue from sales of transmission and reserves fell from \$3.2 million in 2001 to \$2.2 million in 2002. The decline in revenue in these categories was partially offset by revenue from new sources. The Department’s contract with Bonneville that took effect on October 1, 2001, provides credits for investments in conservation and renewable resources. These credits amounted to \$2.1 million in 2002. Revenue from integration and exchange services provided to Pacific Power Management in connection with the purchase of energy from the State Line Wind Project amounted to \$2.8 million. The Department recognized \$3.3 million in revenue associated with payments received from Bonneville for the purchase of conservation savings. The Department expects to receive \$26.7 million from Bonneville in 2002 and 2003 in payments for the purchase of conservation savings. These payments will be recognized as revenue in equal monthly amounts of \$222,178 over the 10-year period of the Bonneville contract.

Other miscellaneous revenues grew from \$10.8 million in 2001 to \$13.0 million in 2002, an increase of \$2.2 million. Penalties and interest on overdue accounts generated \$2.0 million more in revenue in 2002 than in the prior year, revenues from damages increased \$0.9 million, and revenues from other operations increased \$0.8 million. Net revenue from nonutility operations declined from \$2.1 million in 2001 to \$0.8 million in 2002.

OPERATING EXPENSES

Operating expenses declined from \$657.7 million in 2001 to \$650.6 million in 2002, a reduction of \$7.1 million. Expenses in 2001 reflect the deferral of \$300 million in power costs from 2001 to subsequent years; in 2002 expenses include the amortization of \$100 million of these deferred charges. If the deferral of power costs in 2001 and their amortization in 2002 were excluded from consideration, operating expenses in 2002 would have been \$407.1 million lower than in 2001.

Power and Transmission Costs—Power and transmission expenses in 2002 totalled \$408.9 million, a decrease of \$20.1 million from the 2001 level of \$429.0 million.

Long-term purchased power expenses in 2002 were \$223.7 million, \$72.5 million higher than in the prior year, reflecting the full annual cost of additional contract resources acquired in 2001. The cost of power purchased under the new 10-year contract with Bonneville, which took effect on October 1, 2001, increased from \$66.8 million in 2001, to \$134.8 million. The amount of power delivered increased sharply under the terms of the new contract, from 2,384,896 MWh in 2001 to 4,158,297 MWh in 2002. The cost per unit of power also increased as Bonneville invoked its authority to increase rates under the contract’s Cost Recovery

Adjustment Clause (“CRAC”). Bonneville used the CRAC to increase rates by as much as 46% over the period from October 1, 2001, through December 31, 2002. The Department’s contract for power from the Klamath Falls Cogeneration Project provided 709,520 MWh of power in 2002 at a cost of \$39.7 million. In 2001, 326,104 MWh of power were delivered at a cost of \$18.5 million in the period following the July 1, 2001, effective date of the contract. Deliveries of power from the State Line Wind Project began in January 2002. The Department received 106,493 MWh of power from the project in 2002 at a cost of \$8.9 million. Energy delivered to the Department under exchange agreements, computed using the blended weighted-average cost of power, declined by \$22.1 million, from \$28.0 million in 2001 to \$5.9 million in 2002, reflecting both the lower volume and the lower unit value of exchanged energy. The cost of power purchased from the Lucky Peak Project fell from \$16.0 million in 2001 to \$12.4 million in 2002 as a result of the refinancing of the Lucky Peak Project’s outstanding bonds in June 2002. The cost of power under the Department’s contract with the Grand Coulee Project Hydroelectric Authority was \$7.3 million in 2002, a reduction of \$1.2 million from the 2001 level.

In 2001, the Department expended \$518.8 million for purchases of power in the wholesale market to meet its obligations to serve load. Of this amount, \$300.0 million was deferred to future years, leaving \$218.8 million to be recorded as an expense in 2001. The amount of energy purchased in 2001 was unusually high because the Department’s dependence on market purchases through September 30, 2001, was aggravated by drought conditions in the Northwest region, which drastically reduced the amount of generation at the Department’s hydroelectric facilities. Extremely high prices in Western wholesale markets through May 2001 drove the cost of these market purchases to unprecedented levels. In late 2001, water conditions and market prices in the Northwest returned to more normal levels. In addition, energy from the contract resources that became available in 2001, coupled with the decline in system load in 2001, ensured that the Department would have sufficient power available to meet demand even under adverse water conditions. As a result, in 2002 the amount of power purchased in the wholesale market declined from 2,411,210 MWh to 898,613 MWh. The average price of these purchases declined from \$215.15 per MWh in 2001 to \$25.77 per MWh in 2002. The cost of short-term wholesale power purchases in 2002 was \$23.2 million. The amortization of power costs deferred from 2001 added \$100.0 million to this figure. Given the recognition of both the deferral of 2001 power costs and their amortization in 2002, the cost of short-term purchases shows a decline from \$218.8 million in 2001 to \$123.2 million in 2002, a reduction of \$95.6 million. If power costs had not been deferred and amortized, the decline would have been \$495.6 million.

The costs of operating and maintaining the Department’s hydroelectric generating plants increased from \$17.0 million in 2001 to \$18.5 million in 2002, an increase of 9.0%. An increase of \$1.4 million in fees paid to the Federal Energy Regulatory Commission (“FERC”) accounts for most of the growth from 2001. In 2001, FERC charges were lower than normal due to the receipt of a credit of \$0.8 million. Transmission costs, including both the cost of operating and maintaining the Department’s own transmission lines and the cost of wheeling power over the lines of Bonneville and other utilities, increased from \$25.8 million in 2001 to \$35.4 million in 2002, an increase of \$9.6 million or 36.9%. An October 1, 2001, increase in the transmission rates charged by Bonneville, the principal supplier of transmission services to the Department, accounts for most of this increase.

Other power-related expenses declined by \$8.0 million from 2001 to 2002. In 2001, \$4.1 million was paid to large industrial customers as incentives to reduce consumption; no such payments were made in 2002. The value of energy delivered to the Department through basis transactions declined from \$4.4 million in 2001 to \$1.3 million in 2002.

Other Operations and Maintenance Costs—Operations and maintenance costs, excluding the cost of power and transmission, increased from \$114.6 million in 2001 to \$115.0 in 2002, an increase of approximately 0.4%. Increases were experienced in energy management (\$0.6 million) and administration and general activities (\$0.3 million). The increase in conservation largely reflects the amortization of the Department’s investment in energy management programs.

Taxes and Other Intergovernmental Payments—Taxes and payments to local governments totalled \$60.2 million in 2002, an increase of \$7.6 million over the 2001 level. Revenue-based taxes paid to the City of Seattle and the state of Washington increased by \$5.7 million, reflecting the increase in taxable revenue. Payments to suburban cities under the terms of franchise agreements with the Department increased from \$1.6 million to \$2.0 million. In 2001, tax payments were offset by a \$1.2 million refund of arbitrage rebate payments made by the Department to the U.S. Treasury; there was no corresponding transaction in 2002.

Depreciation—Depreciation expense increased from \$61.5 million in 2001 to \$66.5 million in 2002, an increase of \$4.9 million. The increase reflects the impact of the Department's capital improvement program, which in recent years has focused on the replacement of aging plant and equipment and the expansion of capacity in the distribution system to meet customer demand.

NONOPERATING REVENUES AND EXPENSES

Investment Income—Income from the investment of available cash balances totalled \$10.1 million in 2002, a reduction of \$3.2 million from the 2001 level. Declining cash balances and lower interest rates account for the decrease in interest income.

Interest Expense—Debt-related expenses increased from \$75.7 million in 2001 to \$84.1 million in 2002, an increase of \$8.4 million. An increase of \$3.5 million in interest expense on first-lien bonds reflected the issuance of \$503.7 million in revenue bonds and refunding bonds in March 2001, the issuance of \$87.7 million in refunding bonds in December 2002, and the retirement of bonds at their maturity date in 2001 and 2002. Interest expense on second-lien, variable-rate bonds fell from \$3.1 million in 2001 to \$1.4 million in 2002 due to the decline in interest rates over that period. Interest expense for revenue anticipation notes issued by the Department in 2001 and 2002 was \$2.5 million higher in 2002 than in the prior year. Interest on funds borrowed from the City's cash pool was \$0.8 million higher than in 2002. The allowance for funds used during construction, which is a credit against interest expense, was \$2.1 million lower in 2002 than in the prior year. The amortization of deferred charges related to outstanding debt increased by \$0.9 million in 2002.

Contributions, Grants and Transfers—Contributions in aid of construction fell from \$12.5 million in 2001 to \$10.6 million in 2001, reflecting the economic slowdown in the Seattle area. Grants and transfers decreased from \$2.8 million in 2001 to \$2.3 million in 2002. Operating transfers in 2001 included \$0.9 million in funding from the Seattle General Fund for certain low-income and energy efficiency programs; there was no such transfer in 2002. Operating grants fell from \$1.9 million in 2001 to \$0.7 million in 2002. Offsetting these declines, the Department recorded \$1.6 million in donated capital in 2002. There was no such donated capital in 2001.

FINANCIAL POSITION

Significant capital assets and related long-term debt as of December 31:

	2002	2001
SIGNIFICANT CAPITAL ASSETS:		
Utility plant—at original cost:		
Hydraulic	\$ 527,022,003	\$ 522,835,388
Capacity rights—3rd AC Intertie	34,298,665	34,298,665
Transmission	105,652,942	103,141,612
Distribution	1,068,429,863	1,016,151,812
General plant	<u>297,080,942</u>	<u>278,415,352</u>
	2,032,484,415	1,954,842,829
Less accumulated depreciation	<u>(862,964,940)</u>	<u>(808,183,648)</u>
	1,169,519,475	1,146,659,181
Construction work-in-progress	135,358,152	115,321,307
Nonoperating property—net of accumulated depreciation	7,703,571	7,216,228
Land and land rights	<u>32,854,384</u>	<u>30,838,923</u>
	1,345,435,582	1,300,035,639
Parity bond proceeds	<u>66,663,074</u>	<u>166,131,625</u>
	<u>\$1,412,098,656</u>	<u>\$1,466,167,264</u>
SIGNIFICANT LONG-TERM DEBT RELATED TO CAPITAL ASSETS:		
Revenue bonds	\$1,244,693,325	\$1,291,186,426
Bond premium—net	15,374,411	10,983,710
Less deferred charges on advanced refunding	<u>(40,250,704)</u>	<u>(40,215,201)</u>
	<u>\$1,219,817,032</u>	<u>\$1,261,954,935</u>
INVESTED IN CAPITAL ASSETS—NET OF RELATED DEBT	<u>\$ 192,281,624</u>	<u>\$ 204,212,329</u>

CONDENSED BALANCE SHEETS

	December 31, 2002	December 31, 2001
Assets:		
Utility plant	\$ 1,345,435,582	\$ 1,300,035,639
Capitalized purchased power commitment	50,279,621	56,947,942
Restricted assets	240,881,958	243,432,809
Current assets	190,990,153	155,835,416
Other assets	<u>377,433,352</u>	<u>454,709,681</u>
Total assets	<u>\$ 2,205,020,666</u>	<u>\$ 2,210,961,487</u>
Liabilities:		
Long-term debt	\$ 1,365,447,879	\$ 1,683,202,477
Noncurrent liabilities	67,994,521	63,771,698
Current liabilities	452,101,465	143,606,465
Deferred credits	<u>21,216,712</u>	<u>20,255,473</u>
Total liabilities	1,906,760,577	1,910,836,113
Equity:		
Invested in capital assets—net of related debt	192,281,624	204,212,329
Restricted:		
Deferred power costs	200,000,000	300,000,000
Other	66,229,640	35,746,815
Unrestricted	<u>(160,251,175)</u>	<u>(239,833,770)</u>
	<u>298,260,089</u>	<u>300,125,374</u>
Total liabilities and equity	<u>\$ 2,205,020,666</u>	<u>\$ 2,210,961,487</u>

UTILITY PLANT

Utility plant at original cost increased \$77.6 million. The distribution system increased \$52.3 million primarily for data processing-related underground conductors, devices, and conduits (\$22.1 million); overhead, underground, and network underground services (\$6.6 million); and poles, towers, and fixtures (\$6.2 million).

General plant increased \$18.7 million mostly for structures and improvements at the Department's North Service Center (\$7.4 million), communications equipment (\$4.9 million), and automated mapping (\$2.9 million).

Hydroelectric facilities increased \$4.2 million, primarily for rehabilitation work on water wheels and turbines (\$2.3 million) and wildlife and mitigation (\$1.5 million) at the Boundary Project, located on the Pend Oreille River in northeast Washington State.

COST CAPITALIZATION POLICIES

Administration and General Costs ("A&G")—The Department allocates a portion of A&G costs to the Capital Improvement and Conservation Program ("CICP"). A pool of allocable A&G costs is identified and an A&G allocation rate is computed by dividing the projected level of costs in the A&G cost pool in the following year by the projected number of non-A&G direct labor hours. Actual CICP labor hours are

multiplied by the A&G allocation rate and included as a component of a CACP project. A&G costs capitalized were \$19.4 million and \$18.6 million in 2002 and 2001 respectively.

Data Processing Systems—Systems development costs related to major new data processing applications are capitalized.

High Ross—In setting rates for the 2000 – 2003 period, the City of Seattle Council decided to defer the capital portion of the remaining payments to B. C. Hydro under the High Ross agreement over the period through 2035. Previously, the entire amount of the \$21.8 million annual payment was expensed. The deferred portion of the High Ross payments is treated as a component of capital requirements.

Capitalization Limit—The Department of Executive Administration (“DEA”) revised the capitalization limit for the City of Seattle from \$1,000 to \$5,000 effective for 2002. The effect of this change is an increase of approximately \$2.0 million of charges, which were expensed in 2002 rather than capitalized.

SFAS NO. 71 ASSETS

Statement of Financial Accounting Standards (“SFAS”) No. 71, *Accounting for the Effects of Certain Types of Regulations*, provides for the deferral of certain utility costs and related recognition in future years as the costs are recovered through future rates. Deferred costs are authorized by resolutions passed by the Seattle City Council.

	December 31, 2002	December 31, 2001
Deferred power costs	\$ 200,000,000	\$ 300,000,000
Capitalized energy management services—net	108,005,350	97,179,553
Capitalized relicensing costs	12,764,867	11,079,911
British Columbia—Ross Dam	31,448,059	22,574,618
Unrealized losses from fair valuations of		
Gas price swap		13,860,917
Short-term forward sales of electric energy	3,935,769	915,407
BPA Slice contract true-up payment	10,442,663	
Puget Sound Energy interconnection and substation	2,005,283	2,148,197
Skagit Environmental Endowment	2,115,225	2,232,737
Studies, surveys, and investigations	406,808	102,033
	<u>\$ 371,124,024</u>	<u>\$ 450,093,373</u>

Deferred assets totalled \$371.1 million at December 31, 2002, decreasing \$79.0 million from December 31, 2001. In 2001, \$300.0 million of short-term wholesale power costs were deferred for recovery through future revenues. In 2002, \$100.0 million of the deferred power costs were amortized; the balance of \$200.0 million is expected to be recovered by the end of 2004.

In 2002, \$10.4 million was deferred for the Bonneville Slice contract true-up billing. The Department is subject to true-up payments for the Department’s fixed 4.6676 percentage of actual output and costs of Bonneville Slice power through October 1, 2011. Bonneville rate adjustments will be passed through to retail electric customers in the form of rate adjustments in accordance with the rates ordinance.

LONG-TERM DEBT

Activity during the year for long-term debt included issuance of \$87.735 million in refunding revenue bonds to defease certain prior lien bonds. Scheduled redemption of certain prior lien bonds also took place in the normal course of business. See Note 3 of the accompanying financial statements.

After payment of cash operating expenses, net revenues available to pay debt service were equal to 2.51 times principal and interest on first-lien bonds. If, in addition, the amortization of \$100 million in power costs deferred from 2001 is taken into account, net revenues would be equal to 1.61 times first-lien debt service.

ENVIRONMENTAL LIABILITIES

Environmental liabilities totalled \$2.6 million at December 31, 2002, with no change from December 31, 2001. The majority of the liability is attributable to the estimated costs of cleaning up contaminated sediments in the lower Duwamish Waterway, which was designated a federal Superfund site by the Environmental Protection Agency in 2001. The Department is one of several responsible parties for this superfund site.

RISK MANAGEMENT

Market Risk—The Department's exposure to market risk is managed by a Risk Management Committee. It is fundamentally risk averse, engaging in market transactions only to meet its load obligations or to lay off surplus energy. Except for strictly limited and closely monitored intra-day trading to take advantage of its hydro storage, the Department does not take market positions in anticipation of generating revenue.

With a significant portion of the Department's revenue expected from wholesale market sales, great emphasis is placed on the management of market risk. Processes, policies, and procedures designed to monitor and control these market risks, including credit risk, are in place, and engagement in the market is strictly governed by those policies. Formal segregation of the roles of the front, middle, and back offices ensures compliance.

The Department measures the market price risk in its portfolio on a weekly basis using a modified net revenue at risk measure that reflects not only price risk, but also the volumetric risk associated with its hydro-dominant power portfolio. Monte Carlo simulation is used to capture financial risk and scenario analysis for stress testing.

With a new portfolio in place since fall 2001, the Department is now long over 2 million MWh even in severe water conditions. This is in stark contrast to the energy crisis, when the Department was short 3.5 million MWh because of the drought. As a net seller in nearly every month of the year even during droughts, the Department's market risk is clearly very different.

The Department's approach to risk management has also changed. Prior to the energy crisis, operations were planned around average hydro conditions; now planning is performed around conditions close to drought until observed precipitation or snow pack surveys indicate otherwise.

While the Department's portfolio includes a gas turbine (a share of the Klamath Falls project), the Department's exposure to changes in the market price of gas is limited, as the Department has the right not to operate its share if the price of gas is too high relative to the price of electricity produced.

The Department mitigates credit risk by ensuring only qualifying counterparties are engaged in power marketing transactions in accordance with the Department's Credit Policy. A Credit Committee has been established to administer the Credit Policy. The Department performs initial credit evaluations for new counterparties and establishes credit limits based on approved criteria within the Credit Policy. Ongoing credit evaluations are performed and credit limits are updated regularly to reflect the current financial condition and credit worthiness of each counterparty.

Self-Insurance—The Department is self-insured, including for terrorism, for casualty losses to its property, for environmental clean-up, and for certain losses arising from third-party claims. Expenses for injuries and damages are estimated and include citywide allocation of incurred but not reported claims.

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

BALANCE SHEETS DECEMBER 31, 2002 AND 2001

ASSETS	2002	2001
UTILITY PLANT—At original cost:		
Plant in service—excluding land	\$ 2,032,484,415	\$ 1,954,842,829
Less accumulated depreciation	<u>(862,964,940)</u>	<u>(808,183,648)</u>
	1,169,519,475	1,146,659,181
Construction work-in-progress	135,358,152	115,321,307
Nonoperating property—net of accumulated depreciation	7,703,571	7,216,228
Land and land rights	<u>32,854,384</u>	<u>30,838,923</u>
	1,345,435,582	1,300,035,639
CAPITALIZED PURCHASED POWER COMMITMENT	50,279,621	56,947,942
RESTRICTED ASSETS:		
Municipal Light & Power Bond Reserve Account:		
Cash and equity in pooled investments	77,975,000	70,993,458
Bond proceeds and other:		
Cash and equity in pooled investments	158,267,512	63,559,476
Investments		102,274,374
Special deposits and other	<u>4,639,446</u>	<u>6,605,501</u>
	240,881,958	243,432,809
CURRENT ASSETS:		
Cash and equity in pooled investments	34,694,513	3,759,018
Accounts receivable, net of allowance of \$6,690,000 and \$6,110,000	73,345,049	53,187,620
Unbilled revenues	60,079,107	61,366,163
Energy contracts	1,848,350	14,526,178
Materials and supplies at average cost	20,447,710	21,810,750
Prepayments, interest receivable, and other	<u>575,424</u>	<u>1,185,687</u>
	190,990,153	155,835,416
OTHER ASSETS:		
Capitalized energy management services—net	108,005,350	97,179,553
Deferred power costs	200,000,000	300,000,000
Capitalized relicensing costs	12,764,867	11,079,911
Other deferred charges and assets—net	<u>56,663,135</u>	<u>46,450,217</u>
	377,433,352	454,709,681
	<hr/>	<hr/>
TOTAL	<u>\$ 2,205,020,666</u>	<u>\$ 2,210,961,487</u>

See notes to financial statements.

LIABILITIES	2002	2001
LONG-TERM DEBT:		
Revenue bonds and anticipation notes	\$ 1,429,186,000	\$ 1,651,872,500
Plus bond premium—net	17,127,583	13,196,678
Less deferred charges on advanced refunding	(40,250,704)	(40,215,201)
Less revenue bonds—current portion	(40,615,000)	(41,651,500)
Note payable—City of Seattle		<u>100,000,000</u>
	1,365,447,879	1,683,202,477
NONCURRENT LIABILITIES:		
Accumulated provision for injuries and damages	7,895,490	6,125,305
Compensated absences	9,819,410	9,568,451
Long-term purchased power obligation	50,279,621	56,947,942
Less obligation—current portion		<u>(8,870,000)</u>
	67,994,521	63,771,698
CURRENT LIABILITIES:		
Accounts payable and other	71,842,294	51,006,948
Accrued payroll and related taxes	4,668,171	3,820,619
Compensated absences	846,948	642,345
Accrued interest	21,531,101	22,802,987
Revenue anticipation notes	307,210,000	
Long-term debt	40,615,000	41,651,500
Purchased power obligation		8,870,000
Energy contracts	<u>5,387,951</u>	<u>14,812,066</u>
	452,101,465	143,606,465
DEFERRED CREDITS	<u>21,216,712</u>	<u>20,255,473</u>
Total liabilities	1,906,760,577	1,910,836,113
COMMITMENTS AND CONTINGENCIES (Notes 3, 6, and 10)		
EQUITY:		
Invested in capital assets—net of related debt	192,281,624	204,212,329
Restricted:		
Deferred power costs	200,000,000	300,000,000
Other	66,229,640	35,746,815
Unrestricted	<u>(160,251,175)</u>	<u>(239,833,770)</u>
	298,260,089	300,125,374
TOTAL	<u>\$ 2,205,020,666</u>	<u>\$ 2,210,961,487</u>

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN EQUITY YEARS ENDED DECEMBER 31, 2002 AND 2001

	2002	2001
OPERATING REVENUES:		
Retail power revenues	\$ 562,432,218	\$ 503,437,272
Short-term wholesale power revenues	112,795,762	73,899,346
Other power-related revenues	21,110,534	44,303,333
Other	12,991,925	10,814,019
	<u>709,330,439</u>	<u>632,453,970</u>
OPERATING EXPENSES:		
Long-term purchased power	223,668,647	151,213,357
Short-term wholesale power purchases	23,153,996	218,781,800
Amortization of deferred power costs	100,000,000	
Other power expenses	8,147,996	16,143,942
Generation	18,546,296	17,012,159
Transmission	35,352,620	25,820,801
Distribution	37,649,578	38,122,827
Customer service	27,566,006	27,539,641
Energy management	9,514,572	8,887,010
Administrative and general—net	40,315,379	40,030,657
City of Seattle occupation tax	33,913,510	30,648,911
Other taxes	26,260,379	21,916,749
Depreciation	66,485,780	61,538,960
	<u>650,574,759</u>	<u>657,656,814</u>
Net operating income (loss)	58,755,680	(25,202,844)
NONOPERATING REVENUES (EXPENSES):		
Investment income	10,110,004	13,275,220
Interest expense	(81,340,397)	(73,873,786)
Amortization of debt expense	(2,717,316)	(1,786,694)
Other income (expense)—net	357,968	(1,048,013)
	<u>(73,589,741)</u>	<u>(63,433,273)</u>
Net loss before fees, grants, and transfers	(14,834,061)	(88,636,117)
FEES, GRANTS, AND TRANSFERS:		
Capital contributions	10,631,017	12,489,627
Grants and transfers	2,337,759	2,806,083
	<u>12,968,776</u>	<u>15,295,710</u>
NET LOSS	(1,865,285)	(73,340,407)
EQUITY:		
Beginning of year	<u>300,125,374</u>	<u>373,465,781</u>
End of year	<u>\$ 298,260,089</u>	<u>\$ 300,125,374</u>

See notes to financial statements.

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2002 AND 2001

	2002	2001
OPERATING ACTIVITIES:		
Cash received from customers and counterparties	\$ 692,482,007	\$ 671,289,411
Cash paid to suppliers, employees, and counterparties	(394,011,051)	(931,423,126)
Taxes paid	<u>(59,423,235)</u>	<u>(50,134,407)</u>
Net cash provided by (used in) operating activities	239,047,721	(310,268,122)
NONCAPITAL FINANCING ACTIVITIES:		
Proceeds from RAN and City of Seattle note	125,922,862	284,999,427
Principal paid on City of Seattle note	(100,000,000)	
Interest paid on RAN and City of Seattle note	(11,451,300)	(4,223,087)
Grant revenues received	1,289,390	1,014,343
Operating transfers received from the City of Seattle	<u></u>	<u>315,000</u>
Net cash provided by noncapital financing activities	15,760,952	282,105,683
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Proceeds from long-term debt—net	88,247,757	513,343,978
Bond issue costs paid	(585,657)	(2,095,805)
Principal paid on long-term debt	(128,211,500)	(138,030,000)
Interest paid on long-term debt	(74,984,816)	(65,539,492)
Acquisition and construction of capital assets	(133,586,924)	(149,335,107)
Proceeds from sale of other capital assets	763,624	476,683
Capital fees	<u>11,578,573</u>	<u>12,394,505</u>
Net cash (used in) provided by capital and related financing activities	(236,778,943)	171,214,762
INVESTING ACTIVITIES:		
Proceeds from long-term loans receivable	137,933	250,441
Long-term loans issued	(8,137)	(116,765)
Proceeds from sale of investments	216,780,918	567,239,517
Purchases of investments	(114,511,442)	(656,263,060)
Interest received on investments	<u>10,230,016</u>	<u>11,280,508</u>
Net cash provided by (used in) investing activities	<u>112,629,288</u>	<u>(77,609,359)</u>
NET INCREASE IN CASH AND EQUITY IN POOLED INVESTMENTS	130,659,018	65,442,964
CASH AND EQUITY IN POOLED INVESTMENTS:		
Beginning of year	<u>144,917,453</u>	<u>79,474,489</u>
End of year	<u>\$ 275,576,471</u>	<u>\$ 144,917,453</u>

(Continued)

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2002 AND 2001

	2002	2001
RECONCILIATION OF NET OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:		
Net operating income (loss)	\$ 58,755,680	\$ (25,202,844)
Adjustments to reconcile net operating income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	76,288,439	70,412,288
Amortization of deferred power costs	100,000,000	
Cash (used in) provided by changes in operating assets and liabilities:		
Accounts receivable	(15,586,755)	30,981,472
Unbilled revenues	1,287,056	(25,928,733)
Materials and supplies	3,895,411	315,615
Prepayments, interest receivable, and other	(571,654)	10,087,199
Capitalized relicensing and other deferred	12,210,283	(316,162,037)
Provision for injuries and damages	1,770,185	(327,102)
Accounts payable, accrued payroll, and other	6,800,764	(65,068,412)
Compensated absences	13,006	761,547
Energy contracts and deferred credits	(5,814,694)	9,862,885
Net cash provided by (used in) operating activities	<u>\$ 239,047,721</u>	<u>\$ (310,268,122)</u>
CASH AND EQUITY IN POOLED INVESTMENTS AT DECEMBER 31 CONSISTS OF:		
Cash and cash equivalents	\$ 92,215,085	\$ 13,653,054
Equity in pooled investments	<u>183,361,386</u>	<u>131,264,399</u>
	<u>\$ 275,576,471</u>	<u>\$ 144,917,453</u>
SCHEDULE OF NONCASH ACTIVITIES:		
Fair value adjustments of long-term investments	<u>\$ —</u>	<u>\$ 4,897</u>
In-kind capital contributions	<u>\$ 1,566,788</u>	<u>\$ —</u>

See notes to financial statements.

(Concluded)

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2002 AND 2001

NOTE 1. OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City Light Department (the “Department”) is the public electric utility of the City of Seattle (the “City”). The Department owns and operates certain generating, transmission, and distribution facilities and supplies electricity to approximately 360,600 customers. The Department supplies electrical energy to other City agencies at rates prescribed by City ordinances. The establishment of the Department’s rates is within the exclusive jurisdiction of the City of Seattle Council. A requirement of Washington State law provides that rates must be fair, nondiscriminatory, and fixed to produce revenue adequate to pay for operation and maintenance expenses and to meet all debt service requirements payable from such revenue. The Department pays occupation taxes to the City based on total revenues.

The Department also provides nonenergy services to other City funds and received \$2.3 million in 2002 and \$5.8 million in 2001 for such services. Included in accounts receivable at December 31, 2002 and 2001, are \$2.6 million and \$1.1 million, respectively, representing amounts due from other City funds for services provided, reimbursements, and interest receivable on cash and equity in pooled investments.

The Department receives certain services from other City funds and paid approximately \$37.9 million and \$35.2 million, respectively, in 2002 and 2001 for such services. Included in accounts payable for the same time periods are \$6.6 million and \$4.5 million, respectively, representing amounts due other City funds for goods and services received.

Accounting Standards—The accounting and reporting policies of the Department are regulated by the Washington State Auditor’s Office, Division of Municipal Corporations, and are based on the Uniform System of Accounts prescribed for public utilities and licensees by the Federal Energy Regulatory Commission (“FERC”). The financial statements are also prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board (“GASB”) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Department has applied all applicable GASB pronouncements as well as the following pronouncements, except for those that conflict with or contradict GASB pronouncements: Statements and Interpretations of the Financial Accounting Standards Board (“FASB”), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures. The more significant of the Department’s accounting policies are described below.

In June 1999, GASB issued GASB Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, adopted by the Department in 2002 with the following amendments: GASB Statement No. 37, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments: Omnibus—an Amendment of GASB Statements No. 21 and No. 34*, and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. GASB Statement No. 34, as amended, and GASB Statement No. 38 establish specific standards for external financial reporting for state and local governments. As a result of adopting these statements, the basic financial statement presentation was significantly changed, including adding management’s discussion and analysis of operating, investing, and financing activities. GASB

Statement No. 34 also requires the classification of fund equity into three components – invested in capital assets, net of related debt; restricted; and unrestricted, defined as follows:

- *Invested in capital assets, net of related debt* consists of capital assets, net of accumulated depreciation reduced by the net outstanding debt balances.
- *Restricted net assets* has constraints placed on use, either externally or internally. Constraints include those imposed by creditors (such as through debt covenants), grants, or laws and regulations of other governments, or by law through constitutional provisions or enabling legislation or by the Seattle City Council.
- *Unrestricted net assets (deficit)* consists of assets and liabilities that do not meet the definition of “restricted net assets” or “invested in capital assets, net of related debt.”

Under GASB Statement No. 34, the statement of operations and changes in retained earnings was renamed the statement of revenues, expenses, and changes in equity.

In June 2001, the FASB issued Statement of Financial Accounting Standards (“SFAS”) No. 143, *Accounting for Asset Retirement Obligations*. The objective of the statement is to address financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The statement is effective for the Department in 2003, and the Department is in the process of evaluating the financial impact of the statement.

In August 2001, the FASB issued SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, which supercedes SFAS No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*. SFAS No. 144 retains the basic provisions of SFAS No. 121 for the measurement and recognition of the impairment of long-lived assets to be held and used, as well as the measurement of long-lived assets to be disposed of by sale. SFAS No. 144 resolves significant implementation issues related to SFAS No. 121 and retains the amendments in SFAS No. 121 pertaining to regulatory assets under SFAS No. 71 and SFAS No. 90, *Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs*. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001, and was adopted by the Department in 2002 without an impact to financial position or operations.

In April 2002, the FASB issued SFAS No. 145, *Rescission of FASB Statements Nos. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections*. SFAS No. 145 rescinds various pronouncements regarding early extinguishment of debt and allows extraordinary accounting treatment for early extinguishment only when the provisions of Accounting Principles Board Opinion No. 30, *Reporting the Results of Operations, Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions* have been met. SFAS No. 145 provisions regarding early extinguishment of debt are generally effective for the Department for advance refundings using cash and are effective for the Department in 2003. For advance refundings made by issuance of new bonds, the transactions are accounted for in accordance with GASB Statement No. 7, *Advance Refundings Resulting in Defeasance of Debt* and GASB Statement No. 23, *Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary Activities*. The Department does not anticipate a material impact on financial position or operations as a result of adopting SFAS No. 145.

Nonexchange Transactions—In December 1998, GASB issued GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, which requires reporting nonexchange transactions as revenues effective for periods beginning after June 15, 2000. Capital fees from private sources were reported as a component of equity as contributions in aid of construction prior to

implementation of GASB Statement No. 33. Capital fees, grants, and transfers in the amount of \$13.0 million and \$15.3 million are reported for 2002 and 2001 on the statements of revenues, expenses, and changes in equity as nonoperating revenues as a result of the adoption of this statement.

Derivative Instruments—In June 1998, FASB issued SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*. This statement was amended in June 2000 by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities*. Both statements are effective for fiscal years beginning after June 15, 2000, and were adopted by the Department in 2001. SFAS Nos. 133 and 138 require that the fair value of derivative financial instruments be recognized as either assets or liabilities on the Department's balance sheet and that changes in the fair value of a derivative instrument be included in earnings. The Department has outstanding sales and purchases of electric energy under short-term forward contracts for electricity that meet the definition of a derivative in accordance with SFAS No. 133. In addition, the Department entered into a fixed for variable natural gas price swap in April 2001 to fix the fuel expense for the Klamath Falls Cogeneration Project from July 2001 through December 2002 and recognized \$12.3 million and \$6.9 million in 2002 and 2001, respectively, for swap settlements that are reported in long-term purchased power expenses. Derivative values by balance sheet caption as of December 31 are as follows:

	2002	2001
Current assets:		
Energy contracts:		
Forward energy sales	\$ 1,452,182	\$ 14,526,178
Forward energy purchases	<u>396,168</u>	<u> </u>
	1,848,350	14,526,178
Other assets:		
Other deferred charges—net:		
Unrealized losses from fair valuation of:		
Gas price swap		13,860,917
Forward energy sales	3,935,769	
Forward energy purchases	<u> </u>	<u>915,407</u>
	<u>\$ 5,784,119</u>	<u>\$ 29,302,502</u>
Current liabilities:		
Gas price swap	\$ —	\$ 13,860,917
Forward energy sales	5,387,951	35,742
Forward energy purchases	<u> </u>	<u>915,407</u>
	5,387,951	14,812,066
Deferred credits:		
Unrealized gains from fair valuation of:		
Forward energy sales		14,490,436
Forward energy purchases	<u>396,168</u>	<u> </u>
	<u>\$ 5,784,119</u>	<u>\$ 29,302,502</u>

In accordance with Seattle City Council Resolution 30290, deferred losses are regulatory assets, and deferred gains are regulatory liabilities, pursuant to SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*. Thus, SFAS Nos. 133 and 138 have no current year impact on recorded earnings.

The Department's conclusions regarding the accounting treatment and financial statement effect of SFAS No. 133 could change based on interpretations of issues pending before the FASB.

Utility Plant—Utility plant is recorded at original cost, which includes both direct costs of construction or acquisition and indirect costs, including an allowance for funds used during construction. The allowance represents the estimated costs of financing construction projects and is computed using the Department's long-term borrowing rate. The allowance totalled \$3.6 million and \$5.7 million in 2002 and 2001, respectively, and is reflected as a reduction of interest expense in the statements of revenues, expenses, and changes in equity. Property constructed with capital fees received from customers is included in utility plant. Capital fees totalled \$10.6 million in 2002 and \$12.5 million in 2001. Provision for depreciation is made using the straight-line method based upon estimated economic lives, which range from three to 50 years, of related operating assets. The Department uses a half-year convention method on the assumption that additions and replacements are placed in service at mid-year. The composite depreciation rate was approximately 3.3% in 2002 and 3.2% in 2001. When operating plant assets are retired, their original cost together with removal costs, less salvage, is charged to accumulated depreciation. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized.

Utility plant in service at original cost, excluding land, at December 31, 2002, consists of:

	Hydraulic Production	Transmission	Distribution	General	Total
Beginning balance	\$ 522,835,388	\$ 137,440,277	\$ 1,016,151,812	\$ 278,415,352	\$ 1,954,842,829
Capital acquisitions	5,824,060	3,332,380	57,041,644	22,452,494	88,650,578
Dispositions	(1,637,445)	(821,049)	(3,534,867)	(3,786,905)	(9,780,266)
Transfers and adjustments			(1,228,726)		(1,228,726)
	527,022,003	139,951,608	1,068,429,863	297,080,941	2,032,484,415
Less accumulated depreciation	(275,296,702)	(60,272,213)	(383,433,656)	(143,962,369)	(862,964,940)
Ending balance	<u>\$ 251,725,301</u>	<u>\$ 79,679,395</u>	<u>\$ 684,996,207</u>	<u>\$ 153,118,572</u>	<u>\$ 1,169,519,475</u>

FERC licenses for owned hydraulic production facilities consist of:

Project	License Issued	License Effective	License Expires	Years Licensed
Boundary	07/10/1960	10/01/1960	10/01/2010	50
Gorge	05/16/1995	05/01/1995	05/01/2025	30
Diablo	05/16/1995	05/01/1995	05/01/2025	30
Ross	05/16/1995	05/01/1995	05/01/2025	30
Newhalem	02/07/1997	02/01/1997	02/01/2027	30
South Fork Tolt	03/29/1984	03/01/1984	03/01/2024	40

Restricted Assets—In accordance with the Department's bond resolutions, state law, or other agreements, separate restricted assets have been established. These assets are restricted for specific purposes, including the establishment of the Municipal Light & Power ("ML&P") Bond Reserve Account, financing of the Department's ongoing Capital Improvement Program, and other purposes.

Accounts Receivable—Accounts receivable at December 31 consists of:

	2002	2001
Retail power	\$ 57,304,001	\$ 42,520,721
Allowance for doubtful accounts	<u>(4,000,000)</u>	<u>(3,500,000)</u>
	53,304,001	39,020,721
Wholesale power	13,950,626	6,538,072
Allowance for doubtful accounts	<u>(1,520,000)</u>	<u>(1,520,000)</u>
	12,430,626	5,018,072
Fees, grants, and other	4,693,499	6,704,916
Allowance for doubtful accounts	<u>(1,170,000)</u>	<u>(1,090,000)</u>
	3,523,499	5,614,916
Interfund	2,626,871	1,100,652
Due from other governments	<u>1,460,052</u>	<u>2,433,259</u>
	<u>\$ 73,345,049</u>	<u>\$ 53,187,620</u>

Compensated Absences—Permanent employees of the Department earn vacation time in accordance with length of service. A maximum of 480 hours may be accumulated and, upon termination, employees are entitled to compensation for unused vacation. At retirement, employees receive compensation equivalent to 25% of their accumulated sick leave. The Department accrues all costs associated with compensated absences, including payroll taxes.

Accounts Payable and Other—The composition of accounts payable and other at December 31, is as follows:

	2002	2001
Vouchers payable	\$ 10,090,145	\$ 8,544,835
Power accounts payable	40,354,341	25,263,010
Interfund payable	6,566,460	4,527,245
Taxes payable	8,541,055	8,396,449
Claims payable—current	2,580,752	1,965,511
Guarantee deposit and contract retainer	1,998,070	1,767,583
Other accounts payable	<u>1,711,471</u>	<u>542,315</u>
	<u>\$ 71,842,294</u>	<u>\$ 51,006,948</u>

Revenue Recognition—Service rates are authorized by City ordinances. Billings are made to customers on a monthly or bimonthly basis. Revenues for energy delivered to customers between the last billing date and the end of the year are estimated and reflected in the accompanying financial statements under the caption unbilled revenues.

The Department's customer base comprises four identifiable groups, which accounted for electric energy sales as follows:

	2002	2001
Residential	37.6 %	37.3 %
Commercial	42.3	41.6
Industrial	11.2	12.3
Governmental	<u>8.9</u>	<u>8.8</u>
	<u>100.0 %</u>	<u>100.0 %</u>

Use of Estimates—The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements. The Department used significant estimates in determining reported unbilled revenues, energy contract assets and liabilities, accumulated provision for injuries and damages, allowance for doubtful accounts, accrued sick leave, and other contingencies. Actual results may differ from those estimates.

Significant Risk and Uncertainty—The Department is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include prices on the wholesale markets for short-term power transactions; interest rates; water conditions, weather, and natural disaster related disruptions; terrorism; collective bargaining labor disputes; fish and other Endangered Species Act ("ESA") issues; Environmental Protection Agency regulations; federal government regulations or orders concerning the operations, maintenance, and/or licensing of hydroelectric facilities; other governmental regulations; and the deregulation of the electrical utility industry.

Reclassifications—Certain 2001 account balances have been reclassified to conform to the 2002 presentation.

NOTE 2. CASH AND EQUITY IN POOLED INVESTMENTS AND INVESTMENTS

Cash and Equity in Pooled Investments and Investments—The City pools and invests all temporary cash surpluses for City departments. These residual investments may consist of deposits with qualified public depositories; obligations of the United States or its agencies or wholly owned corporations; obligations of eligible government-sponsored enterprises; and certain bankers' acceptances, commercial paper, general obligation bonds or warrants, repurchase agreements, reverse repurchase agreements, mortgage-backed securities, derivative-based securities, and participation in the State Treasurer's local government investment pool and are in accordance with the Revised Code of Washington 35.39.032 and 39.58. According to City policy, securities purchased will have a maximum maturity of no longer than 15 years, and the average maturity of all securities owned should be no longer than five years. Also by City policy, the City may operate a securities lending program, and there were transactions during 2002 and 2001. There were no securities lending program transactions outstanding at year end 2002 or 2001. The Department's equity in residual investments is reflected as cash and equity in pooled investments. The City's residual investment pool did not include reverse repurchase agreements at the end of 2002 or 2001; the City did not invest in such instruments during 2002 or 2001. Derivative-based securities were owned by the City pool during 2002 and 2001 and at both year ends. These securities were callable U.S. government agency instruments. Earnings and adjustments to fair value from the investment pool are prorated monthly to City departments based on the average daily cash balances of participating funds.

Banks or trust companies acting as the City's agents hold most of the City's investments in the City's name, with respect to credit risk as defined in GASB Statement No. 3, *Deposits with Financial*

Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements. All transactions are executed with authorized security dealers, financial institutions, or securities lending agents on a delivery versus payment basis.

The first \$100,000 of bank deposits are federally insured. The Washington State Public Deposit Protection Commission (“PDPC”) collateralizes deposits in excess of \$100,000. The PDPC is a multiple financial institution collateral pool. There is no provision for the PDPC to make additional pro rata assessments if needed to cover a loss. Therefore, the PDPC protection is of the nature of collateral, not of insurance.

Securities with maturities exceeding three months at time of purchase are reported at fair value on the balance sheets; the net increase (decrease) in the fair value of those investments is reported as part of investment income. At December 31, changes in the fair value of investments resulted in unrealized gains of \$817,806 and \$907,046 for 2002 and 2001, respectively.

The cash pool operates like a demand deposit account in that all City departments, including the Department, may deposit cash at any time and can also withdraw cash out of the pool without prior notice or penalty. Accordingly, the statements of cash flows reconcile to cash and equity in pooled investments.

Cash and cash equivalents included in cash and equity in pooled investments at December 31 consists of:

	2002	2001
Restricted assets:		
Municipal Light & Power Bond Reserve Account	\$ 24,998,402	\$ 3,609,215
Bond proceeds and other	51,152,110	3,236,017
Special deposits and other	<u>4,639,446</u>	<u>6,605,501</u>
	80,789,958	13,450,733
Current assets	<u>11,425,127</u>	<u>202,321</u>
	<u><u>\$ 92,215,085</u></u>	<u><u>\$ 13,653,054</u></u>

Equity in pooled investments and U.S. government securities are reported at fair values based on quoted market prices for those or similar securities and is as follows at December 31:

	2002	2001
Restricted assets:		
Municipal Light & Power Bond Reserve Account—		
Equity in pooled investments	\$ 52,976,598	\$ 67,384,243
Bond proceeds and other:		
Equity in pooled investments	107,115,402	60,323,459
Investments	<u>102,274,374</u>	<u>102,274,374</u>
	160,092,000	229,982,076
Current assets:		
Equity in pooled investments	<u>23,269,386</u>	<u>3,556,697</u>
	<u><u>\$ 183,361,386</u></u>	<u><u>\$ 233,538,773</u></u>

NOTE 3. LONG-TERM AND SHORT-TERM DEBT

At December 31, the Department's long-term and short-term debt consists of the following:

LONG-TERM				2002	2001
Prior Lien Bonds:					
2002	ML&P Refunding Revenue Bonds	3.000% to 4.500%	due 2014	\$ 87,735,000	\$ —
2001	ML&P Improvements and Refunding Revenue Bonds	5.000% to 5.500%	due 2026	503,700,000	503,700,000
2000	ML&P Revenue Bonds	4.500% to 5.625%	due 2025	98,830,000	98,830,000
1999	ML&P Revenue Bonds	5.000% to 6.000%	due 2024	158,000,000	158,000,000
1998B	ML&P Revenue Bonds	4.750% to 5.000%	due 2024	90,000,000	90,000,000
1998A	ML&P Refunding Revenue Bonds	4.500% to 5.000%	due 2020	102,835,000	103,515,000
1997	ML&P Revenue Bonds	5.000% to 5.125%	due 2022	30,000,000	30,000,000
1996	ML&P Revenue Bonds	5.250% to 5.625%	due 2021	29,135,000	30,000,000
1995B	ML&P Revenue Bonds	4.050% to 4.800%	due 2005	456,000	697,500
1995A	ML&P Revenue Bonds	5.000% to 5.700%	due 2020	55,815,000	56,665,000
1994	ML&P Revenue Bonds	6.00%	due 2004	6,280,000	9,385,000
1993	ML&P Revenue & Refunding Revenue Bonds	2.200% to 5.500%	due 2018	166,360,000	237,135,000
1992B	ML&P Revenue Bonds	2.750% to 5.750%	due 2010	—	48,335,000
				<u>1,329,146,000</u>	<u>1,366,262,500</u>
Subordinate Lien Bonds:					
1996	ML&P Adjustable Rate Revenue Bonds	variable	due 2021	19,140,000	19,800,000
1993	ML&P Adjustable Rate Revenue Bonds	variable	due 2018	18,700,000	19,600,000
1991B	ML&P Adjustable Rate Revenue Bonds	variable	due 2016	17,500,000	18,300,000
1991A	ML&P Adjustable Rate Revenue Bonds	variable	due 2016	25,000,000	25,000,000
1990	ML&P Adjustable Rate Revenue Bonds	variable	due 2015	<u>19,700,000</u>	<u>20,700,000</u>
				100,040,000	103,400,000
Revenue Anticipation Notes—					
2001	ML&P Revenue Anticipation Notes	4.500% and 5.250%	due 2003	—	182,210,000
City of Seattle Note Payable—2001 Note Payable		variable	due 2004	<u>—</u>	<u>100,000,000</u>
Total long-term debt				<u>\$ 1,429,186,000</u>	<u>\$ 1,751,872,500</u>
SHORT-TERM					
Revenue Anticipation Notes:					
2001	ML&P Revenue Anticipation Notes	4.500% and 5.250%	due 2003	\$ 182,210,000	\$ —
2002	ML&P Revenue Anticipation Notes	2.500%	due 2003	<u>125,000,000</u>	<u>—</u>
Total short-term debt				<u>\$ 307,210,000</u>	<u>\$ —</u>

The Department had the following activity in long-term debt during 2002:

	Balance at December 31, 2001	Additions	Reductions	Balance at December 31, 2002	Current Portion
Prior Lien Bonds	\$ 1,366,262,500	\$ 87,735,000	\$(124,851,500)	\$ 1,329,146,000	\$ 37,030,000
Subordinate Lien Bonds	103,400,000		(3,360,000)	100,040,000	3,585,000
Revenue Anticipation Notes	182,210,000		(182,210,000)		
Note payable—City of Seattle	100,000,000		(100,000,000)		
	<u>\$ 1,751,872,500</u>	<u>\$ 87,735,000</u>	<u>\$(410,421,500)</u>	<u>\$ 1,429,186,000</u>	<u>\$ 40,615,000</u>

Prior Lien Bonds—In December 2002, the Department issued \$87.7 million in ML&P Refunding Revenue Bonds that bear interest at rates ranging from 3.00% to 4.50% and mature serially from December 1, 2003, through 2014. The arbitrage yield for the 2002 bonds is 3.427%. Arbitrage yield, when used in computing the present worth of all payments of principal and interest on the bonds, produces an amount equal to the issue price of the bonds. Proceeds were used to defease certain outstanding prior lien bonds. The debt service on the refunding bonds requires a cash flow of \$110.4 million, including \$22.7 million in interest. The difference between the cash flows required to service the old and the new debt and complete the refunding totalled \$5.1 million, and the aggregate economic gain totalled \$5.97 million at net present value. The loss on refunding was \$8.9 million and is being amortized over the life of the new bonds. The unamortized balance of the loss on refunding at December 31, 2002, is \$8.8 million.

In March 2001, the Department issued \$503.7 million in ML&P Improvements and Refunding Revenue Bonds that bear interest at rates ranging from 5.00% to 5.50% and mature serially from March 1, 2004, through 2026. The arbitrage yield for the 2001 bonds is 4.99%. Proceeds were used to finance certain capital improvements and conservation programs and to defease certain outstanding prior lien bonds. As of the end of December 31, 2002 and 2001, respectively, \$61.4 million and \$161.7 million in proceeds remained from the 2001 bond issue that were and will continue to be used to fund the ongoing capital improvement and conservation program. The loss on refunding for the 2001 bonds was \$9.4 million and is being amortized over the life of the new bonds. The unamortized balance of the loss on refunding at December 31, 2002 and 2001, was \$8.6 million and \$9.2 million, respectively.

The debt service on the 2001 refunding bonds requires a cash flow of \$194.67 million, including \$70.07 million in interest. The difference between the cash flows required to service the old and the new debt and complete the refunding totalled \$(0.3) million, and the aggregate economic gain totalled \$5.13 million at net present value.

Future debt service requirements for prior-lien bonds are as follows:

Year Ending December 31,	Principal Redemptions	Interest Requirements	Total
2003	\$ 37,030,000	\$ 69,338,346	\$ 106,368,346
2004	48,100,000	67,340,816	115,440,816
2005	49,936,000	64,862,402	114,798,402
2006	53,480,000	62,460,798	115,940,798
2007	56,145,000	59,792,255	115,937,255
2008 – 2012	307,035,000	253,251,731	560,286,731
2013 – 2017	318,200,000	169,534,350	487,734,350
2018 – 2022	287,070,000	86,532,170	373,602,170
2023 – 2026	<u>172,150,000</u>	<u>17,138,284</u>	<u>189,288,284</u>
	<u>\$1,329,146,000</u>	<u>\$ 850,251,152</u>	<u>\$2,179,397,152</u>

The Department is required by ordinance to fund reserves for prior lien bond issues in an amount equal to the lesser of (a) the maximum annual debt service on all bonds secured by the reserve account or (b) the maximum amount permitted by the Internal Revenue Code (“IRC”) of 1986 as a reasonably required reserve or replacement fund. Upon issuance of the 2002 bonds, the maximum annual debt service on prior lien bonds remained at \$115.9 million. The IRC’s requirement increased from \$105.6 million to \$113.5. At December 31, 2002, the balance in the reserve account was \$78.0 million at fair value. The reserve must be fully funded by December 1, 2007.

In addition to the 2002 refunding revenue bonds, the Department has previously issued several refunding revenue bonds for the purpose of defeasing certain outstanding prior lien bonds. Refunding revenue bonds were also issued in 2001, 1998, and 1993. Proceeds from the refunding bonds were placed in separate irrevocable trusts to provide for all future debt service payments on the bonds defeased. Accordingly, neither the assets of the respective trust accounts nor the liabilities for the defeased bonds are reflected in the Department’s financial statements. The bonds defeased in 2002, 1998, and 1993 had outstanding principal balances of \$86.6 million, \$94.7 million, and \$6.3 million as of December 31, 2002, respectively. Funds held in the respective trust accounts on December 31, 2002, are sufficient to service and redeem the defeased bonds.

Subordinate Lien Bonds—The Department is authorized to issue a limited amount of adjustable rate revenue bonds, which are subordinate to prior lien bonds with respect to claim on revenues. Subordinate lien bonds may be issued to the extent that the new bonds will not cause the aggregate principal amount of such bonds then outstanding to exceed the greater of \$70 million or 15% of the aggregate principal amount of prior lien bonds then outstanding. Subordinate bonds may be remarketed daily, weekly, short-term, or long-term and may be converted to prior lien bonds when certain conditions are met.

In December 1996, the Department issued ML&P Adjustable Rate Revenue Bonds in the amount of \$19.8 million, subject to a mandatory redemption schedule spanning the period from June 1, 2002, to June 1, 2021. The bonds had an outstanding balance of \$19.1 million at December 31, 2002. These bonds were marketed weekly at an interest rate ranging from 1.00% to 1.80% during 2002. Proceeds were used to finance a portion of the capital improvement and conservation program.

The 1990 bonds and 1991 Series B bonds were marketed on a short-term basis during 2002, with interest rates ranging from 1.10% to 2.65%. The 1990 bonds and the 1991 Series B bonds had an outstanding balance of \$19.7 million and \$17.5 million, respectively, at December 31, 2002.

The 1991 Series A bonds and the 1993 bonds were priced weekly at interest rates from 0.88% to 1.80% in 2002. The 1991 Series A bonds and the 1993 bonds had an outstanding balance of \$25.0 million and \$18.7 million, respectively, at December 31, 2002.

Future debt service requirements on these bonds, based on actual interest rates in effect as of December 31, 2002, ranging from 1.20% to 1.51% through year 2021, are as follows:

Year Ending December 31,	Principal Redemptions	Interest Requirements	Total
2003	\$ 3,585,000	\$ 1,571,284	\$ 5,156,284
2004	4,115,000	1,336,089	5,451,089
2005	4,445,000	1,294,522	5,739,522
2006	4,775,000	1,216,303	5,991,303
2007	5,305,000	1,149,689	6,454,689
2008 - 2012	33,945,000	4,511,193	38,456,193
2013 - 2017	37,055,000	1,740,723	38,795,723
2018 - 2021	<u>6,815,000</u>	<u>178,431</u>	<u>6,993,431</u>
	<u>\$ 100,040,000</u>	<u>\$ 12,998,234</u>	<u>\$ 113,038,234</u>

Revenue Anticipation Notes—In November 2002, the Department issued \$125.0 million in ML&P Revenue Anticipation Notes (“RANs”) at an interest rate of 2.50% with an arbitrage yield of 1.49%. The 2002 RANs mature in November 2003.

In March 2001, the Department issued \$182.2 million in ML&P RANs. \$136.7 million of the 2001 RANs bear interest at a rate of 4.50%, and \$45.5 million bear interest at a rate of 5.25%. The arbitrage yield of the 2001 RANs is 3.75%. The 2001 RANs mature in March 2003.

All RANs are special limited obligations of the Department payable from and secured by gross revenues. Proceeds were used to finance operating expenses for each respective year. The RANs are on a lien subordinate to prior lien bonds and subordinate lien bonds; there is no reserve account securing repayment, and there is no debt service coverage requirement. Debt service requirements for the RANs are as follows:

Year Ending December 31,	Principal Redemptions	Interest Requirements	Total
2003	<u>\$ 307,210,000</u>	<u>\$ 7,324,362</u>	<u>\$ 314,534,362</u>

Fair Value—The fair value of the Department’s bonds and RANs is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to the Department for debt of the same remaining maturities. Carrying amounts and fair values are as follows at December 31:

	2002		2001	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt:				
Prior lien bonds	\$1,344,779,509	\$1,407,056,096	\$1,377,523,172	\$1,385,989,653
Subordinate				
lien bonds	99,780,904	100,040,000	103,123,038	103,400,000
RANs	<u>308,963,171</u>	<u>309,942,021</u>	<u>184,422,967</u>	<u>186,594,405</u>
	<u>\$1,753,523,584</u>	<u>\$1,817,038,117</u>	<u>\$1,665,069,177</u>	<u>\$1,675,984,058</u>

Amortization—Bond issue costs, discounts, and premiums are amortized using the effective interest method over the term of the bonds.

The excess of costs incurred over the carrying value of bonds refunded on early extinguishment of debt is amortized as a component of interest expense using both the straight-line and bonds-outstanding methods over the terms of the issues to which they pertain. Deferred refunding costs amortized to interest expense totalled \$4.2 million in 2002 and \$2.1 million in 2001. Deferred refunding costs in the amount of \$40.3 million and \$40.2 million are reported as a component of long-term debt in the 2002 and 2001 balance sheets, respectively.

Note Payable—In late December 2001, the City authorized an interfund loan (note payable) to the Department from the City’s Consolidated (Residual) Cash Portfolio in an amount up to \$110.0 million, of which \$100.0 million was outstanding as of December 31, 2001. The purpose of the note payable was for working capital and was due on or before March 31, 2003. The loan was repaid on January 1, 2002, and was carried as a negative operating cash balance during part of 2002. The loan was repaid as of December 31, 2002, and may be carried as a negative operating cash balance in 2003 until maturity. The interest rate for the note payable was equal to the rate of return earned by the City’s Consolidated (Residual) Cash Portfolio in 2002 or 4.238%.

NOTE 4. SEATTLE CITY EMPLOYEES’ RETIREMENT SYSTEM

The Seattle City Employees’ Retirement System (“SCERS”) is a single-employer defined benefit, public employee retirement system, covering employees of the City and administered in accordance with Chapter 41.28 of the Revised Code of Washington and Chapter 4.36 of the Seattle Municipal Code. SCERS is a pension trust fund of the City.

All employees of the City are eligible for membership in SCERS with the exception of uniformed police and fire personnel who are covered under a retirement system administered by the state of Washington. Employees of Metro (“King County”) and the King County Health Department who established membership in SCERS when these organizations were City departments were allowed to continue their SCERS membership. As of the actuarial valuation date, there were 4,858 annuitants receiving benefits and 8,353 active members of SCERS. In addition, 1,199 vested terminated employees were entitled to future benefits, and 185 terminated employees had restored their contributions due to the provisions of the portability statutes and may be eligible for future benefits.

SCERS provides retirement, death, and disability benefits. Retirement benefits vest after five years of credited service, while death and disability benefits vest after 10 years of service. Retirement benefits are calculated as 2% multiplied by years of creditable service, multiplied by average salary, based on the

highest 24 consecutive months, excluding overtime. The benefit is actuarially reduced for early retirement.

Actuarially recommended contribution rates both for members and for the employer were 8.03% of covered payroll during 2002 and 2001.

Under the authority of the state and City, SCERS operates a securities lending program, and there were transactions during 2002 and 2001. SCERS has had no losses resulting from a default, and SCERS did not have negative credit exposure at December 31, 2002 or December 31, 2001.

SCERS issues stand-alone financial statements that may be obtained by writing to the Seattle City Employees' Retirement System, 801 Third Avenue, Suite 300, Seattle, Washington 98104; telephone: (206) 386-1292.

Employer contributions for the City were \$36.6 million and \$32.7 million in 2002 and 2001, respectively, and the annual required contributions were made in full. The recent performance of the stock market has increased the Unfunded Actuarial Accrued Liabilities ("UAAL") of SCERS. It is not known whether employer contributions will be necessary in the foreseeable future to fund a portion of SCERS's UAAL.

Actuarial data

Valuation date	January 1, 2002
Actuarial cost method	Entry age
Amortization method	Level percent
Remaining amortization period	33.7 years
Amortization period	Open
Asset valuation method	Fair market value

Actuarial assumptions*

Percentage

Investment rate of return	8.00%
Projected general wage increases	4.50
Cost-of-living year-end bonus dividend	0.67

* Underlying price inflation at 4.0%.

Schedule of funding progress for the City (dollar amounts in millions):

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liabilities ("AAL") Entry Age (1)	Unfunded AAL ("UAAL") (2)	Funding Ratio (a/b)	Covered Payroll (3)	UAAL or Excess as a Percentage of Covered Payroll ((b-a)/c)
January 1,	(a)	(b)	(b-a)		(c)	
2000	\$ 1,582.7	\$ 1,403.1	\$ (179.6)	112.8 %	\$ 370.4	(48.5)%
2001(4)	1,493.1	1,490.3	(2.8)	100.2	405.0	(.7)
2002	1,383.7	1,581.4	197.7	87.5	405.1	48.8

- (1) Actuarial present value of benefits less actuarial present value of future normal costs based on entry age actuarial cost method.
- (2) Actuarial accrued liabilities less actuarial value of assets; funding excess if negative.

- (3) Covered payroll includes compensation paid to all active employees on which contributions are calculated.
- (4) Information for January 1, 2001, was provided by an actuarial study, rather than a full valuation.

NOTE 5. DEFERRED COMPENSATION

The Department's employees may contribute to the City's Voluntary Deferred Compensation Plan (the "Plan"). The Plan, available to City employees and officers, permits participants to defer a portion of their salary until future years. The deferred compensation is paid to participants and their beneficiaries upon termination, retirement, death, or unforeseeable emergency.

Effective January 1, 1999, the Plan became an eligible deferred compensation plan under Section 457 of the IRC of 1986, as amended, and a trust exempt from tax under IRC Sections 457(g) and 501(a). The Plan is operated for the exclusive benefit of participants and their beneficiaries. No part of the corpus or income of the Plan shall revert to the City or be used for, or diverted to, purposes other than the exclusive benefit of participants and their beneficiaries.

The Plan is not reported in the financial statements of the City or the Department.

It is the opinion of the City's legal counsel that the City has no liability for investment losses under the Plan. Participants direct the investment of their money into one or more options provided by the Plan and may change their selection from time to time. By enrolling in the Plan, participants accept and assume all risks inherent in the Plan and its administration.

NOTE 6. LONG-TERM PURCHASED POWER WHOLESALE POWER TRANSACTIONS AND TRANSMISSION

Bonneville Power Administration—The Department purchased electric energy from the U.S. Department of Energy, Bonneville Power Administration ("Bonneville") under a long-term contract, which expired September 30, 2001.

Until August 1, 1996, the Department was entitled to buy from Bonneville the energy required to fill the variance between its customer load and its firm power resources. The Department had a right to displace this entitlement, by payment of an availability charge. Effective August 1, 1996, the contract with Bonneville was amended, through the remaining life of the contract, to limit purchases to 195 average megawatts ("aMW") delivered flat throughout the year. The Department could displace part of this amount by paying an availability charge; almost no Bonneville energy was displaced in 2001. Power purchased under this contract was 195.0 aMW through September 30, 2001. The 1996 contract amendment required payment of a diversity fee of \$2.0 million, which was amortized through September 30, 2001.

In October 2000, the Department entered into a new agreement to purchase power from Bonneville for a 10-year period beginning October 1, 2001, under the Block and Slice Power Sales Agreement. Under the terms of the agreement the Department received firm power of 152.3 aMW and 5.7 aMW in 2002 and 2001, respectively, and will receive 145.4 aMW in the third through fifth years of the contract and 259.5 aMW in the last five years of the contract as a block of power shaped to the Department's monthly net requirements, defined as the difference between projected monthly load and firm resources available to serve that load. Additional amounts of power will be purchased and received throughout the term of the contract under the Slice portion of the contract. The terms of the Slice product specify that the Department will receive a fixed percentage (4.6676%) of the actual output of the Federal Columbia River Power System. The cost of Slice power is based on the same percentage (4.6676%) of the expected costs of the system and is subject to true-up adjustments based on actual costs. The true-up adjustment billed by Bonneville for 2002 was \$10.4 million, which was deferred pending rate recovery of the amount due. The Department received 322.4 aMW and 71.5 aMW of energy through the Slice

product in 2002 and 2001, respectively. Under critical water conditions, the Department is expected to receive 330.0 aMW for the remaining term of the contract from the Slice product. The actual amounts of firm and nonfirm energy will vary with water conditions, federal generating capabilities, and fish and wildlife restoration requirements.

Amendments to the contract through November 2002 provide that Bonneville will pay the Department for energy savings through specified programs. The conservation augmentation program provides Bonneville funding for a portion of the Department's conservation costs in exchange for a reduction of the amount of power, by the amount of energy saved, that the Department will purchase from Bonneville. The Department received \$20.0 million in cash through December 31, 2002, and will receive a total of \$26.7 million through December 2003. The total amount of payments received is being recognized over the life of the Bonneville contract and \$3.3 million was recognized in 2002. The reduction of energy associated with conservation augmentation was 9.0 aMW in the first year of the contract. The conservation and renewables discount program provides a Bonneville power bill credit for qualifying conservation, renewables, and low-income weatherization costs and donations to qualifying organizations. In 2002, \$2.1 million was received in conservation and renewable discounts, and in 2001, \$0.5 million was received.

In 1983, the Department entered into separate net billing agreements with Bonneville and Energy Northwest (formerly the Washington Public Power Supply System), a municipal corporation and joint operating agency of the state of Washington, with respect to sharing costs for the construction and operation of three nuclear generating plants. Under these agreements, the Department is unconditionally obligated to pay Energy Northwest a pro rata share of the total annual costs, including debt service, decommissioning costs and asset retirement obligations, to finance the cost of construction, whether or not construction is completed, delayed, or terminated, or operation is suspended or curtailed. The net billing agreements provide that these costs be recovered through Bonneville rates. The Department pays the amounts billed by Bonneville directly to Energy Northwest until the payment obligation has been fulfilled for the year. The billings for the remainder of the year are then paid to Bonneville. One plant is in commercial operation. Construction of the other two plants has been terminated.

Lucky Peak—In 1984, the Department entered into a purchase power agreement with four irrigation districts to acquire 100% of the net output of a hydroelectric facility that began commercial operation in 1988 at the existing Army Corps of Engineers Lucky Peak Dam on the Boise River near Boise, Idaho. The irrigation districts are owners and license holders of the project, and the FERC license expires in 2030. The agreement, which expires in 2038, obligates the Department to pay all ownership and operating costs, including debt service, over the term of the contract, whether or not the plant is operating or operable.

The power purchased under this agreement was 33.0 aMW and 21.5 aMW in 2002 and 2001, respectively. To properly reflect its rights and obligations under this agreement, the Department includes as an asset and liability the outstanding principal of the project's debt, net of the balance in the project's reserve account. In July 2002, the project issued revenue refunding bonds totalling \$55.985 million that bear interest ranging from 3.0% to 5.0% and mature July 1, 2004, through 2008.

British Columbia—Ross Dam—In 1984, an agreement was reached between the Province of British Columbia and the City under which British Columbia will provide the Department with power equivalent to that which would result from an addition to the height of Ross Dam. The agreement was ratified through a treaty between Canada and the United States in the same year. The power is to be received for 80 years, and delivery of power began in 1986. The Department will make annual payments to British Columbia of \$21.8 million through 2020, which represent the estimated debt service costs the Department would have incurred had the addition been constructed. The payments are charged to expense over a period of 50 years through 2035.

The Department is also paying equivalent operation and maintenance costs. Payments made for this purpose totalled \$163,997 and \$160,774 in 2002 and 2001, respectively. The power purchased under this agreement was 33.9 aMW and 35.1 aMW of energy and up to 141.0 megawatts (“MW”) and 143.0 MW of peak capacity in 2002 and 2001, respectively.

In addition to the direct costs of power under the agreement, the Department incurred costs of approximately \$8.0 million in prior years related to the proposed addition and was obligated to help fund the Skagit Environmental Endowment Commission through four annual \$1.0 million payments. These costs were deferred and are being amortized to purchased power expense over 35 years.

Klamath Falls—In November 2000, the Department and the City of Klamath Falls, Oregon, entered into an agreement for the purchase of energy and capacity from the Klamath Falls Cogeneration Project, a 500 MW unit consisting of two combustion turbines fueled by natural gas and a steam generator. Under the terms of the contract, the Department receives 100.0 MW of capacity from the project beginning on the project’s online date of July 29, 2001, through July 31, 2006, with an option to renew the contract for an additional five years. The Department may elect to displace all or a portion of the energy it is entitled to receive from this project in any given month. The power purchased under this agreement was 81.0 aMW in 2002 and 37.2 aMW in 2001. The Department assumes gas price and exchange rate risks for natural gas from Alberta, Canada. In April 2001, the Department entered into a separate contract that expired in December 2002 to swap variable Canadian dollar gas prices for a fixed U.S. dollar gas price.

Wind Generation—In October 2001, the Department entered into three agreements with Pacific Corp Power Marketing, Inc. (“PPMI”) for the purchase of energy and associated environmental attributes primarily from the State Line Wind Project, a facility consisting of 399 660-kW wind turbines located in Walla Walla County, Washington, and Umatilla County, Oregon. 16.1 aMW of energy was generated in 2002. The aggregate maximum delivery rate per hour was 50 MW through July 31, 2002, increasing to 100 MW from August 1, 2002, through December 31, 2021. The Department will also receive additional firm energy with an aggregate maximum delivery rate per hour of 25 MW from January 1, 2004, through June 30, 2004, and 50 MW from July 1, 2004, through December 31, 2021, from the State Line Wind Project or another qualifying wind generation facility. PPMI may deliver, at its option, additional energy with a maximum delivery rate per hour of 25 MW beginning in 2004 from other qualifying wind generation projects.

The Department entered into a related 10-year agreement to purchase integration and exchange services from Pacific Corp. Pacific Corp receives State Line Wind Project energy at the Wallula Substation in Walla Walla County, Washington, and stores, reshapes, and delivers the power two months later. The Department also entered into another related 20-year agreement to sell integration and exchange services to PPMI.

Other Long-Term Purchased Power Agreements—The Department also purchases energy from Public Utility Districts (the “PUDs”) No. 1 of Pend Oreille County and No. 2 of Grant County (“Grant County PUD”), under agreements expiring October 31, 2005; the Grand Coulee Project Hydroelectric Authority (the “GCPH Authority”), which includes the South, East, and Quincy Columbia Basin Irrigation Districts (“SCBID”) under 40-year agreements that expire from 2022 to 2027; and the Columbia Storage Power Exchange (“CSPE”), until expiration of the agreement on March 31, 2003. Power purchased under these contracts was 81.9 aMW in 2002 and 77.4 aMW in 2001. Rates under the Grant County PUD and GCPH Authority contracts represent the share of the operating and debt service costs in proportion to the share of total energy to which the Department is entitled, whether or not these plants are operating or operable.

Three new contracts were executed in March 2002 with Grant County PUD to replace the contract expiring October 31, 2005. The agreements are effective November 1, 2005, and run concurrent with the term of the future federal relicense period.

Transmission—In July 2000, the Department entered into an agreement with Bonneville for firm transmission service under Bonneville’s open access transmission tariff from August 2000 through July 2025. In September 1994, the Department entered into an agreement with Bonneville for ownership of 160 MWh of Bonneville’s Pacific Northwest north-south AC Intertie for \$34.3 million and annual operations costs. Other transmission contracts were executed in 1995 with Puget Sound Energy for transmission of South Fork Tolt power through 2020; in 1988 with Idaho Power for transmission of Lucky Peak power through December 2007; in 1983 with GCPHA (formerly “SCBID”) for transmission of the output of the GCPHA’s power plants over the 40-year terms of several related power contracts; and in 1983 (as amended in 1990) with Avista for transmission of the power output of the Summer Falls and Main Canal projects through October 2005.

Estimated Future Payments Under Purchased Power And Transmission Contracts—The Department’s estimated payments under its contracts with Bonneville; the PUDs; irrigation districts; power exchange corporation; Lucky Peak Project; British Columbia – Ross Dam; Klamath Falls; with PPMI and PacifiCorp for wind energy and net integration and exchange services; and for transmission for the period from 2003 through 2035, undiscounted, are:

Year ending December 31,	Estimated Payments
2003	\$ 266,705,346
2004	295,205,580
2005	304,098,377
2006	292,723,786
2007	300,146,326
2008 – 2012 ⁽¹⁾	1,138,794,034
2013 – 2017	436,432,564
2018 – 2022	380,247,545
2023 – 2027 ⁽²⁾	129,021,666
2028 – 2032	13,172,884
2033 – 2035	641,435
	<u>\$3,557,189,543</u>

(1) Bonneville Block and Slice contract expires October 1, 2011.

(2) Bonneville Transmission contract expires July 31, 2025.

The effects of a proposed Regional Transmission Organization and other changes that could occur to transmission as a result of FERC’s proposed Standard Market Design are not reflected in the estimated future payments.

Payments in 2002 under these long-term power contracts totalled \$238.2 million; and payments under the transmission agreements amounted to \$30.7 million. Energy received represented 99.6% of the Department’s total purchases under firm power contracts during 2002.

Wholesale Power Transactions—Power transactions in response to seasonal resource and demand variations include purchases and sales under short-term agreements and exchanges of power under long- and short-term contracts. Fluctuations in annual precipitation levels and other weather conditions materially affect the energy output from the Department’s hydroelectric facilities and some of its long-term purchased power agreements. Accordingly, power transactions required to manage the Department’s load and dispose of surplus energy may vary from year to year. Following are short-term wholesale power contract commitments outstanding at December 31:

	2002	2001
Wholesale power purchases outstanding:	\$ 2,940,900	\$ 2,880,600
Megawatt hours (“MWh”)	88,800	91,800
Average contract purchase cost per MWh	33.12	31.38
Wholesale power sales outstanding:	54,206,420	42,703,580
MWh	1,570,000	1,137,000
Average contract sales price per MWh	34.53	37.56

In March 1998, the Department was certified as a scheduling coordinator with the California Independent System Operator to submit schedules and sell power and ancillary services in California. The effects of proposed Regional Transmission Organization and other changes that could occur to transmission design are not reflected in the forecast.

NOTE 7. OTHER ASSETS

Other assets comprise deferred energy management costs and other deferred charges. Deferred energy management costs, net, represent programmatic conservation costs. Seattle City Council-passed resolutions authorize the debt financing and deferral of programmatic conservation costs not funded by third parties and incurred by the Department. These costs are to be recovered through rates over 20 years.

Other deferred charges, net, consist of the following at December 31:

	2002	2001
British Columbia—Ross Dam	\$ 31,448,059	\$ 22,574,618
BPA Slice contract true-up payment	10,442,663	
Puget Sound Energy interconnection and substation	2,005,283	2,148,197
Skagit Environmental Endowment	2,115,225	2,232,737
Studies, surveys, and investigations	406,808	102,033
Real estate and conservation loans receivable	657,441	277,500
Unrealized losses from fair valuations of:		
Gas price swap		13,860,917
Short-term forward sales of electric energy	3,935,769	915,407
Unamortized debt expense	4,461,726	4,103,307
General work in process to be billed	1,036,565	1,124,420
Other	153,596	(888,919)
	<u>\$ 56,663,135</u>	<u>\$ 46,450,217</u>

Deferred power costs incurred for short-term wholesale power purchases during 2001 are expected to be recovered through rates at \$8.3 million per month through 2004, pursuant to SFAS No. 71 and Ordinance 120385. Unamortized charges for the deferral of debt payments relating to Ross Dam will be

amortized between 2021 and 2035. The remaining components of other assets, excluding billable work in progress, are being amortized to expense over four to 36 years.

NOTE 8. DEFERRED CREDITS

Deferred credits consists of the following at December 31:

	2002	2001
BPA conservation augmentation	\$ 16,663,356	\$ —
Unrealized gains from fair valuation of short-term forward sales of electric energy	396,168	14,490,436
Levelized lease payments for Seattle office	947,360	1,263,337
Prepaid capital fees	1,732,238	1,819,000
Customer deposits—sundry sales	1,070,531	1,183,708
Prepaid grants	164,785	398,000
Unspent transfer from the City	144,204	965,977
Other	98,070	135,015
	<u>\$ 21,216,712</u>	<u>\$ 20,255,473</u>

NOTE 9. PROVISION FOR INJURIES AND DAMAGES

The Department is self-insured for casualty losses to its property, including for terrorism, environmental cleanup, and certain losses arising from third-party damage claims. The Department establishes liabilities for claims based on estimates of the ultimate cost of claims. The length of time for which such costs must be estimated varies depending on the nature of the claim. Actual claims costs depend on such factors as inflation, changes in doctrines of legal liability, damage awards, and specific incremental claim adjustment expenses. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates, which reflect recent settlements, claim frequency, industry averages, City-wide cost allocations, and economic and social factors. Liabilities for lawsuits, claims, and workers' compensation were discounted over a period of 15 to 17 years in 2002 and 11 to 16 years in 2001 at the City's average annual rate of return on investments, which was 4.238% in 2002 and 5.341% in 2001. Liabilities for environmental cleanup and for casualty losses to the Department's property do not include claims that have been incurred but not reported and are not discounted due to uncertainty with respect to regulatory requirements and settlement dates, respectively.

The schedule below presents the changes in the provision for injuries and damages during 2002 and 2001:

	2002	2001
Unpaid claims at January 1	\$ 8,090,816	\$ 8,023,794
Payments	(1,474,499)	(2,664,709)
Incurred claims	<u>3,859,925</u>	<u>2,731,731</u>
Unpaid claims at December 31	<u>\$ 10,476,242</u>	<u>\$ 8,090,816</u>

The provision for injuries and damages is included in current and noncurrent liabilities as follows:

	2002	2001
Noncurrent liabilities	\$ 7,895,490	\$ 6,125,305
Accounts payable and other	<u>2,580,752</u>	<u>1,965,511</u>
	<u>\$ 10,476,242</u>	<u>\$ 8,090,816</u>

NOTE 10. COMMITMENTS AND CONTINGENCIES

Operating Leases—In December 1994, the City entered into an agreement on behalf of the Department for a 10-year lease of office facilities in downtown Seattle commencing February 1, 1996. In early 1996, the City purchased the building in which these facilities are located, thus becoming the Department's lessor.

The Department also has two other long-term operating leases for smaller facilities used for office and storage purposes.

Expense under the leases totalled \$3.5 million and \$3.3 million in 2002 and 2001, respectively. Deferred credits related to the 10-year lease of office facilities in downtown Seattle totalled \$0.9 million and \$1.3 million at December 31, 2002 and 2001, respectively.

Minimum payments under the leases are:

Year Ending December 31,	Minimum Payments
2003	\$ 3,488,500
2004	3,360,971
2005	3,371,641
2006	280,970
2007	
	<u>\$ 10,502,082</u>

Skagit Mitigation—In 1995, FERC issued a license for operation of the Skagit Project in effect through 2025. As a condition of the license, the Department has taken and will continue to take various mitigating actions relating to fisheries, wildlife, erosion control, archeology, historic preservation, recreation, and visual quality issues. The mitigation cost was estimated at December 31, 2002, to be \$52.3 million of which \$37.2 million has been expended.

2003 Program—The estimated financial requirement for the Department's 2003 capital improvement and conservation program is \$145.5 million, and the Department has substantial contractual commitments relating thereto.

Project Impact Payments—Effective November 1999, the Department committed to pay a total of \$11.6 million and \$7.8 million over 10 years ending in 2008 to Pend Oreille County and Whatcom County, respectively, for impacts on county governments from the operations of the Department's hydroelectric projects. The payments compensate the counties, and certain school districts and towns located in these counties, for loss of revenues and additional financial burdens associated with the projects. The Boundary Project located on the Pend Oreille River affects Pend Oreille County, and Skagit River hydroelectric projects affect Whatcom County. The combined impact compensation and retroactive

payments totalled \$1.1 million to Pend Oreille County and \$0.7 million to Whatcom County in each year of 2002 and 2001.

Endangered Species—Some fish species that inhabit waters where hydroelectric projects are owned by the Department or where the Department purchases power have been listed under the ESA as either threatened or endangered. In 1995, the National Marine Fisheries Service (“NMFS”) developed a broad species recovery plan for the Columbia River Basin and supplemental plans in 1998 and 2000, based on biological opinions relating to the Columbia and Snake River fisheries. As a result, the Department’s power generation at its Boundary Project has been reduced in the fall and winter when the region experiences its highest sustained energy demand, and the Boundary Project’s firm capability has also been reduced. The U.S. Fish & Wildlife Service released a draft recovery plan for Bull Trout in late 2002. The Department has provided comments and is planning to continue to work with the agency as the plan is developed. In addition, the Department now receives power under a contract with Bonneville that provides the City with a percentage of the total Bonneville generation and the Department would thus be affected by changes in flows required in the biological opinions. In the opinion of the Department, it is unlikely that new biological opinions will result in significant changes in flows that would affect the Boundary Project, Priest Rapids, and Bonneville system. While it is unclear how other fish listings, including bull trout and chinook salmon, may affect the Department’s hydroelectric projects and operations, the Department has entered into agreements that include extensive measures to protect fish and were intended to mitigate potential impacts of its projects on the Cedar, Skagit, and South Fork Tolt rivers. In addition, the Department is conducting research on these species to monitor their population health and identify potential impacts. The Department is carrying out an ESA Early Action program that will assist in the recovery of chinook and bull trout and address any further impacts on these species.

All hydroelectric projects must satisfy the requirements of the Clean Water Act to obtain a FERC license. An agreement was reached for the Newhalem Creek plant on minimum stream flows necessary to protect fish; these flows were incorporated into the FERC license issued in 1997. The Department has installed a new intake system capable of delivering the approved instream flows. The completion of the intake system, including all improvements and testing, was reported to FERC in August 2001. The new system has been performing reliably since this time.

* * * * *

APPENDIX D

DEMOGRAPHIC AND ECONOMIC INFORMATION

(This page intentionally left blank.)

DEMOGRAPHIC AND ECONOMIC INFORMATION

King, Snohomish and Island Counties constitute the Seattle-Bellevue-Everett Primary Metropolitan Statistical Area (the "Seattle PMSA"), the fourth-largest metropolitan center on the West Coast. The City of Seattle, encompassing 92 square miles, is the largest city in the Pacific Northwest and is the center of King County's economic activity. Of the State's population, nearly 30 percent reside in King County, and of the County's population, 33 percent live in the City.

Population

The 1990 and 2000 U.S. Census population figures and recent population estimates for the City, King County and the Seattle PMSA are as follows:

Year	Seattle	King County	Seattle PMSA
2002 ⁽ⁱⁱ⁾	570,800	1,774,300	NA
2001 ⁽ⁱⁱ⁾	568,100	1,758,300	NA
2000 ⁽ⁱ⁾	563,374	1,737,034	2,414,616
1999 ⁽ⁱⁱ⁾	540,500	1,677,000	2,333,600
1998 ⁽ⁱⁱ⁾	539,700	1,665,800	2,306,400
1990 ⁽ⁱ⁾	516,259	1,507,319	1,972,961

(i) Source: U.S. Census

(ii) Source: Washington State Office of Financial Management, Forecasting Division

Per Capita Income

The following table presents per capita personal income. Per capita income for the State of Washington in 2001 was \$32,025.

	2000	1999	1998	1997	1996
Seattle PMSA	\$ 40,686	\$ 38,858	\$ 35,880	\$ 32,766	\$ 30,775
King County	45,536	43,201	39,335	35,382	33,316
State of Washington	31,230	29,819	28,285	26,469	25,015

Source: U.S. Bureau of Economic Analysis, U.S. Department of Commerce

Building Permit Value

The table below lists the value of housing construction for which building permits have been issued by the City of Seattle. The value of public construction is not included in this table.

CITY OF SEATTLE BUILDING PERMITS

Year	New Single Family		New Multifamily		Total Value
	Units	Value	Units	Value	
2002*	381	\$ 60,198,048	1,569	\$ 110,661,851	\$ 170,860,259
2001	484	73,945,951	3,162	222,190,662	296,136,613
2000	449	64,587,520	4,403	286,312,450	350,899,970
1999	480	65,696,744	3,065	191,087,633	256,784,377
1998	530	71,640,186	3,534	219,183,170	290,823,356
1997	469	68,601,487	1,930	147,134,120	215,735,607

* Through September 2002.

Source: Building Permit Activity of City and County in the State of Washington, BP Logistics

Industry and Employment

The table below shows employment by sector and unemployment for the Seattle PMSA.

**SEATTLE-BELLEVUE-EVERETT PMSA
(KING, SNOHOMISH AND ISLAND COUNTIES)
RESIDENT CIVILIAN LABOR FORCE AND EMPLOYMENT
AND NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT**

	Average Annual ⁽¹⁾				
	2001 ⁽²⁾	2000 ⁽³⁾	1999	1998	1997
Civilian Labor Force					
Employment	1,292,600	1,344,500	1,357,200	1,337,300	1,297,500
Unemployment	<u>70,400</u>	<u>52,000</u>	<u>47,600</u>	<u>42,700</u>	<u>44,800</u>
Total Civilian Labor Force	1,362,900	1,396,500	1,404,800	1,380,000	1,342,300
Unemployment Rate ⁽⁴⁾	5.2%	3.7%	3.4%	3.1%	3.3%
Nonagricultural Employment					
Manufacturing					
Aircraft and parts	83,600	82,400	95,100	108,200	101,100
Misc. trans. equipment	6,900	9,100	9,500	9,300	8,800
Food products	14,300	15,200	14,900	16,100	17,000
Wood products and paper	11,900	12,100	12,100	12,500	12,400
Machinery and electrical	21,600	22,100	22,200	21,700	20,700
Instruments	11,500	11,700	11,900	12,100	11,800
Textiles, apparel and leather	4,100	4,400	4,500	4,900	5,100
Printing and publishing	13,600	14,400	13,700	13,800	14,100
Other manufacturing categories	<u>27,900</u>	<u>29,300</u>	<u>30,100</u>	<u>29,700</u>	<u>27,800</u>
Total manufacturing	195,400	200,700	214,000	228,200	218,800
Nonmanufacturing					
Mining and quarrying	1,100	1,100	700	700	700
Contract construction	80,100	84,300	78,400	73,300	66,500
Transp., commun. and utilities	87,100	87,900	84,000	81,000	77,700
Wholesale and retail trade	324,700	335,900	325,000	315,500	304,000
Finance, insurance and real estate	87,400	84,000	84,600	81,500	76,700
Services	429,900	438,000	408,700	390,800	371,400
Government	<u>195,800</u>	<u>190,500</u>	<u>187,000</u>	<u>183,000</u>	<u>178,100</u>
Total nonmanufacturing	1,206,100	1,221,700	1,168,400	1,125,600	1,075,100
Total Nonagricultural Employment	1,401,500	1,422,400	1,382,400	1,353,800	1,293,900

(1) Columns may not add to totals due to rounding.

(2) Preliminary.

(3) Revised.

(4) Unemployment rate as of January 2003 estimated at 6.5 percent.

Source: Washington State Department of Employment Security

The following table presents employment data for major employers in the Puget Sound area, which is defined for the purposes of this section as King, Kitsap, Pierce, and Snohomish Counties, Washington.

**PUGET SOUND AREA
MAJOR EMPLOYERS**

<u>Employer</u>	<u>Employees</u>
The Boeing Company	58,900 ⁽¹⁾
Microsoft	25,235 ⁽²⁾
University of Washington	23,500
King County	14,700
Safeway	12,800
City of Seattle	10,600
Group Health Cooperative	10,000
Sisters of Providence Health	9,600
Weyerhaeuser	8,400
Swedish Health	7,115

(1) State-wide employment as of March 2003. (The Puget Sound area is the location for almost all of the Boeing employment within the State.)

(2) As of July 2002.

Sources: Economic Development Council of Seattle and King County and individual employers, March 2003.

The Boeing Company ("Boeing") had revenues of \$58.0 billion in 1999, \$51.3 billion in 2000 and \$58.2 billion in 2001. Through the third quarter of 2002, revenues were \$40.3 billion, compared to \$42.5 billion through the third quarter of 2001. Total airplane deliveries in 2002 were 381, compared to 527 in 2001. Boeing remains the largest employer in the Puget Sound area, although total employment within the company dropped from 238,600 to 164,300 and employment within the State dropped from 103,420 to 58,900 between February 1998 and March 2003. In September 2001, Boeing moved its corporate headquarters to Chicago, Illinois. Subsequent to the events of September 11, 2001, Boeing laid off or gave notices of layoffs to more than 30,000 employees (as partially reflected in the table above); Boeing announced in December 2002 that it expects to lay off another 5,000 workers in 2003.

Microsoft, which is headquartered in Redmond, is the region's largest high technology employer with more than 50,600 employees worldwide, including 25,205 in the Puget Sound area as of July 26, 2002. Microsoft is a developer and manufacturer of computer operating systems and software. Microsoft's fiscal year 2002 revenues were \$28.4 billion, compared to \$25.3 billion in fiscal year 2001.

Retail Activity

The following table presents taxable retail sales in Seattle and King County.

THE CITY OF SEATTLE AND KING COUNTY TAXABLE RETAIL SALES (000)

<u>Year</u>	<u>The City of Seattle</u>	<u>King County</u>
2002*	\$ 9,345,584	\$ 25,593,133
2001	13,024,765	35,772,850
2000	13,625,486	37,383,541
1999	12,728,470	34,517,504
1998	11,457,199	31,518,255
1997	10,643,911	29,196,029

* Through third quarter of 2002.

Source: *Washington State Department of Revenue*

Other Information

A variety of additional issues may have an effect on the economy of the Seattle area, including but not limited to transportation infrastructure, endangered species listings, the commercial real estate market, higher energy costs, limits on residential development and resulting housing costs, and the September 11, 2001, terrorist attacks and their effect on aerospace, tourism and travel. The effects of these issues are interdependent and cannot be quantified.

APPENDIX E

BOOK-ENTRY TRANSFER SYSTEM

(This page intentionally left blank.)

BOOK-ENTRY TRANSFER SYSTEM

The following information has been provided by DTC. The City makes no representation as to the accuracy or completeness thereof. Purchasers of the Bonds (the “beneficial owners”) should confirm the following with DTC or its participants (the “Participants”).

The Depository Trust Company (“DTC”), New York, New York, will act as securities depository for the Bonds. The Bonds will be issued as fully registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully registered Bond certificate will be issued for the Bonds in the aggregate principal amount of such issue, and will be deposited with DTC.

DTC, the world’s largest depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over two million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges in Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange, LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of the Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co, or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements that may be in effect from time to time.

Redemption notices will be sent to Cede & Co. If less than all of the Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions and dividend payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Bond Registrar, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Bond Registrar or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Bond Registrar, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the City or the Bond Registrar. Under such circumstances, in the event that a successor depository is not obtained, Bond certificates are required to be printed and delivered.

The following information has been provided by the City.

The City may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

Neither the City nor the Bond Registrar will be required to transfer or exchange Bonds during the period between a record date and the next succeeding interest payment date or redemption date. For purposes hereof, record date will mean in the case of each interest payment date, the Bond Registrar's close of business on the 15th day of the month preceding the interest payment date.

With respect to Bonds registered on the Bond Register in the name of DTC or its nominee, the City and the Bond Registrar will have no responsibility or obligation to any Participant or to any person on behalf of whom a Participant holds an interest in the Bonds with respect to (i) the accuracy of the records of DTC, Cede and Co. or any Participant with respect to any ownership interest in the Bonds, (ii) the delivery to any Participant or any other person, other than a bond owner as shown on the Bond Register, of any notice with respect to the Bonds, including any notice of redemption, (iii) the payment to any Participant or any other person, other than a bond owner as shown on the Bond Register, of any amount with respect to principal of or interest on the Bonds, (iv) the selection by DTC or any Participant of any person to receive payment in the event of a partial redemption of the Bonds; (v) any consent given or action taken by DTC as registered owner, or (vi) any other matter. The City and the Bond Registrar may treat and consider Cede and Co., in whose name each bond is registered on the Bond Register, as the holder and absolute owner of such bond for

the purpose of payment of principal and interest with respect to such bond, for the purpose of giving notices of redemption and other matters with respect to such bond, for the purpose of registering transfers with respect to such bond, and for all other purposes whatsoever.

The City's obligations under the Bond Legislation and the Bonds are to the registered owner or owners of the Bonds, and the City will not be liable to the Participants or beneficial owners of Bonds registered in the name of any nominee of DTC or a successor depository, for any acts or omissions of DTC or such successor depository.

(This page intentionally left blank.)

APPENDIX F

SPECIMEN MUNICIPAL BOND INSURANCE POLICY

(This page intentionally left blank.)



**FINANCIAL
SECURITY
ASSURANCE.**

MUNICIPAL BOND INSURANCE POLICY

ISSUER:

BONDS:

Policy No.: -N

Effective Date:

Premium:

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the

United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or teletyped notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud, whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Countersignature]

FINANCIAL SECURITY ASSURANCE INC.

By _____

By _____
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022

(212) 826-0100

Form 500NY (5/90)